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No. 07-

IN THE

Supreme Court of the United States

RIDGE CHRYSLER JEEP, LLC, DOING BUSINESS AS MARQUETTE CHRYSLER JEEP, AND SALES, INCORPORATED, DOING BUSINESS AS DODGE MIDLOTHIAN,

Petitioners

v.

DAIMLERCHRYSLER FINANCIAL SERVICES AMERICAS LLC, FORMERLY KNOWN AS DAIMLERCHRYSLER SERVICES NORTH AMERICA LLC,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the Seventh Circuit erred in applying the less stringent preponderance of the evidence standard, inconsistent with cases from the First, Second, Third, Eighth and D.C. Circuits rather than the more rigorous clear and convincing evidence standard, in determining whether plaintiffs' conduct warranted dismissal as a sanction.

2. Whether the Seventh Circuit erred in affirming the dismissal of the present case as a discovery sanction, rather than allowing the cause to proceed to trial and be decided on the merits by a jury.

STATEMENT PURSUANT TO RULE 29.6

Petitioners Ridge Chrysler Jeep, LLC, d/b/a Marquette Chrysler Jeep, and Sales, Inc., d/b/a Dodge Midlothian have no parent corporations or publicly held companies owning 10% or more of the corporations' stock.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED FOR REVIEW	i
STATEMENT PURSUANT TO RULE 29.6 ...	ii
TABLE OF CONTENTS	iii
TABLE OF APPENDICES	vi
TABLE OF CITED AUTHORITIES	vii
CITATIONS TO OPINIONS BELOW	1
STATEMENT OF JURISDICTION	1
STATUTE INVOLVED	2
STATEMENT OF THE CASE	2
REASONS FOR GRANTING THE PETITION ..	8

I. THE SEVENTH CIRCUIT'S INCORRECT DETERMINATION THAT THE STANDARD TO BE USED IN ASSESSING A DISCOVERY SANCTION IS THE PREPONDERANCE OF THE EVIDENCE, RATHER THAN CLEAR AND CONVINCING EVIDENCE, CONFLICTS WITH TWO OTHER DECISIONS OF THE SEVENTH CIRCUIT AS WELL AS DECISIONS

Contents

Page

OF THE FIRST, SECOND, THIRD, EIGHTH AND D.C. CIRCUITS ON THE SAME ISSUE. 10

A. A Conflict Exists Between The Standard Imposed By The Seventh Circuit In *Ridge* And The Standard Imposed By The First, Second, Third, Eighth and D.C. Circuits. ... 10

B. The Seventh Circuit's Application Of A Preponderance Of The Evidence Standard Of Proof Required To Impose Sanctions In *Ridge* Conflicts With Other Decisions Of The Seventh Circuit Applying A Clear and Convincing Standard of Proof To The Decision To Impose Sanctions. 13

C. The Seventh Circuit's Decision In *Ridge* Disregards The Accepted Analysis Required To Ensure That The Sanction Imposed Is Proportional To The Wrongful Conduct. 17

Contents

Page

II. THE SEVENTH CIRCUIT'S TREND TOWARDS DISMISSING CASES AS A SANCTION, RATHER THAN ENTERING A LESSER SANCTION AND ALLOWING THE CASE TO PROCEED ON THE MERITS, PRESENTS AN IMPORTANT FEDERAL QUESTION ON THE INTERPRETATION OF THE FEDERAL RULES OF CIVIL PROCEDURE. 20

CONCLUSION 23

TABLE OF APPENDICES

Page

Appendix A — Opinion Of The United States Court Of Appeals For The Seventh Circuit Decided February 20, 2008 ..... 1a

Appendix B — Memorandum Opinion And Order Of The United States District Court For The Northern District Of Illinois, Eastern Division Dated September 6, 2006 ..... 10a

Appendix C — Report And Recommendation Of The United States District Court For The Northern District Of Illinois, Eastern Division Filed June 14, 2005 ..... 44a

Appendix D — Relevant Portions Of Federal Rule Of Civil Procedure 37 ..... 96a

Appendix E — Order Of The United States Court Of Appeals For The Seventh Circuit Denying Petition For Rehearing Filed March 17, 2008 ..... 99a

TABLE OF CITED AUTHORITIES

Page

CASES

Allen v. Chicago Transit Authority, 317 F.3d 696 (7th Cir. 2003) 17-18

Aoude v. Mobil Oil Corporation, 892 F.2d 1115 (1st Cir. 1989) 10, 11, 16

Ball v. Chicago, 2 F.3d 752 (7th Cir. 1993) 18

Chambers v. NASCO, Inc., 501 U.S. 32 (1991) .. 20, 22

Forman v. Davis, 371 U.S. 178 (1962) 19, 22

Grogan v. Garner, 498 U.S. 279 (1991) . 14, 15, 16, 17

Herman & MacLean v. Huddleston, 459 U.S. 375 (1983) 14, 15, 16, 17

Link v. Wabash Railroad Comp., 370 U.S. 626 (1962) 22

Maynard v. Nygren, 332 F.3d 462 (7th Cir. 2003) . *passim*

Mickle v. Morin, 297 F.3d 114 (2nd Cir. 2002) ... 11

Pfizer, Inc. v. International Rectified Corp., et al., 538 F.3d 180 (8th Cir. 1976) 11, 16

Roadway Express, Inc. v. Piper, 447 U.S. 752 (1980) 19

Cited Authorities

Page

Scholastic, Inc. v. Stouffer, 21 F. Supp. 2d 425 (S.D.N.Y. 2002) 16

Shepherd v. American Broadcasting Companies, Inc., 62 F.3d 1469 (D.C. Cir. 1995) 11, 12, 15-16, 22

Societe Internationale Pour Participations Industrielles Et Commerciales, S.A. v. Rogers, 357 U.S. 197 (D.C. 1958) 21

Ty, Inc. v. Softbelly's, Inc., 517 F.3d 494 (7th Cir. 2008) ..... *passim*

Wade v. Soo Line Railroad Corp., 500 F.3d 559 (7th Cir. 2007) 16, 20

STATUTES

15 U.S.C. § 1221, *et seq* 2

28 U.S.C. § 1254(1) 2

28 U.S.C. § 1291 2

28 U.S.C. § 1331 2

28 U.S.C. § 1332 2

Cited Authorities

Page

RULE

Fed. R. Civ. P. 37 ..... *passim*

OTHER AUTHORITIES

5B Charles A. Wright & Arthur R. Miller, FEDERAL PRACTICE & PROCEDURE: CIVIL 3rd § 1357 (3rd ed. 1969) 19

Petitioners, Ridge Chrysler Jeep, LLC, doing business as Marquette Chrysler Jeep, and Sales, Incorporated, doing business as Dodge Midlothian (hereinafter "petitioners"), respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit (hereinafter "Seventh Circuit"), entered in this cause on February 20, 2008, as well as the Seventh Circuit's order denying petitioners' Petition for Rehearing, entered on March 17, 2008.[1]

CITATIONS TO OPINIONS BELOW

The decision of the Court of Appeals for the Seventh Circuit is reported at 516 F.3d 623 (7th Cir. 2008), and is reprinted in full in the appendix hereto at Appendix A, 1a –9a.

The Order of the United States District Court for the Northern District of Illinois, Eastern Division (V. Kendall), is reported at 2006 WL 2808158 (N.D. Ill. 2006), and is reprinted in full in the appendix hereto at Appendix B, 10a-43a

STATEMENT OF JURISDICTION

Petitioners seek review of the decision of the Seventh Circuit, entered on February 20, 2008, affirming the District Court's dismissal of Petitioners' claims with prejudice, and awarding costs. The Seventh

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[1] Counsel for Petitioners wish to acknowledge the assistance in the preparation of this Petition For Writ Of Certiorari of law student Victoria Moore.

Circuit found that the District Court did not abuse its discretion in determining that Petitioners' conduct warranted dismissal with prejudice as a sanction. The Seventh Circuit denied Plaintiffs' Petition for Rehearing With Suggestion for Rehearing *En Banc* on March 17, 2008. The District Court had federal question jurisdiction over the present matter under 28 U.S.C. § 1331, as the Complaint alleged violations of the Automobile Dealer's Day in Court Act, 15 U.S.C. § 1221, *et seq.* The District Court also had diversity jurisdiction under 28 U.S.C. § 1332, as all Petitioners are citizens of Illinois, Respondent is a citizen of Delaware and Michigan, and the amount in controversy exceeds $75,000. The Seventh Circuit had jurisdiction to review the District Court's ruling under 28 U.S.C. § 1291 as an appeal of a final decision from the District Court. This Court has jurisdiction to review the Seventh Circuit's decision under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Fed. R. Civ. P. 37 – see Appendix D, 96a-98a for applicable text.

STATEMENT OF THE CASE

This appeal arises out of a breach of contract action, brought by Petitioners Ridge Chrysler Jeep L.L.C. and Sales, Inc. ("Petitioners" or "Ridge"), against Respondent Daimler Chrysler Services North America, L.L.C. ("Respondent" or "Chrysler"). (R. Doc. 1). Chrysler filed a counterclaim against Ridge, adding Gerald W. Gorman ("Gorman") and Elizabeth A. Gorman, his wife, as counter-defendants. (R. Doc. 13).

In February 1999, Gorman purchased the Marquette Chrysler Jeep dealership ("Marquette") located at 6515 South Western Avenue in Chicago, Illinois. The customer base of Marquette was roughly ninety percent (90%) African-American. Prior to this purchase, Gorman had been affiliated with Chrysler Corporation as a Dodge dealership owner since June 1990. (R. Doc. 1, at ¶15).

In September 2000, Gorman purchased the Dodge of Midlothian dealership ("Midlothian") at 14500 South Cicero Avenue in Midlothian, Illinois, just outside of Chicago. The customer base of Midlothian was roughly thirty percent African-American. (R. Doc. 1, at ¶16). Marquette and Midlothian (the "Dealerships") entered into contracts with Chrysler Financial to inventory and sell new and used vehicles manufactured by DaimlerChrysler. (R. Doc. 1, at ¶17; R. Doc. 12, at ¶2). Both Dealerships signed "Financing Agreements" with Defendant Chrysler whereby Chrysler agreed to buy sales contracts from the dealerships. When Chrysler agreed to buy these sales contracts, it provided financing for the dealership customers' vehicle purchases. (R. Doc. 1, at ¶18; R. Doc. 12, at ¶2). Chrysler and the Dealerships also entered into various other financing agreements that, the Complaint alleges, worked impossible hardships on the Dealerships because they were the result of Chrysler's racially biased attitude toward the Dealerships' customer base. (R. Doc. 1, at ¶15-48). This attitude was conveyed to Gorman and others in his

employ by two of Chrysler's Zone Managers, who made such incendiary statements as:

> We found out these 'mulignons' [a derogatory racial slur] were getting [sales contracts] bought and [financing] approved by Chrysler when they should be standing on the bus. And if it weren't for Rosa Parks, those niggers would still be standing in the back of the bus.
>
> (R. Doc. 1, at ¶28).
>
> My whole office knows that I don't buy nigger paper. I might buy some niggers at a suburban store because at least they're smart enough not to get shot while trying to buy a car in the ghetto.
>
> (R. Doc. 1, at ¶29).
>
> What, do you think we have insurance for nigger fraud? The bottom line is you just can't trust these guys and that's why I don't buy nigger paper.
>
> (R. Doc. 1, at ¶43).
>
> Well, you've got to give the nigger a little credit for shopping in the suburbs where the washrooms are cleaner and he has a better chance of getting off the lot with his new ride without getting killed . . . . "A higher class suburban 'shine' is better than those dog ass

f - - -ing south side ghetto pieces of s - - t . . . . To be honest with you, I'd prefer that you not send me one f - - -ing customer from the ghetto.

(R. Doc. 1, at ¶58-59).

Everyone knows how I feel about them, including Detroit. And that's why my delinquencies [losses] are lower than everyone else's and why I run the most profitable Zone in the country – because I don't buy nigger paper.

(R. Doc. 1, at ¶62).

[N]iggers don't pay. Everyone [at Chrysler] knows they don't pay and we've got the statistics to prove it.

(R. Doc. 1, at ¶63).

You see, Chrysler Corp. [the manufacturer] doesn't mind selling cars to these niggers. But we just don't want to finance them. And where I come from, we have a different name for them: We call them 'coons.' One problem ya'll have up here is that you don't have your niggers under control. Down South, where I come from, we keep our niggers under control.

(R. Doc. 1, at ¶73).

> Well guys, what did we decide to do with Gerry's nigger deals? Ha-ha.
>
> (R. Doc. 1, at ¶104).
>
> Gerry, so we have some current and former Chrysler people who like to throw around the 'N-word.' Where does that leave us? How does that hurt you?
>
> (R. Doc. 1, at ¶106).

Throughout the proceedings, Respondent denied these statements. (R. Doc. 12).

In June 2002, a Chrysler Vice-President from Chrysler's national headquarters in Michigan came to Chicago to meet with Gorman. At that meeting, the Chrysler officer presented Gorman with a new and revised set of loan documents, including a "Master Loan Security Agreement", a Notice of Assignment, a Continuing Guaranty, and a Retail Installment Contract and Lease Program Agreement, the terms of which had been greatly altered to the benefit of Chrysler and to the detriment of Petitioners' dealerships. (R. Doc. 1, at ¶94). Gorman was told that if he did not accept the revised terms in the new loan documents, despite their unfair and one-sided nature, Chrysler would pull its financial backing for the floor plan inventory at Midlothian. (R. Doc. 1, at ¶97). Having no choice, Gorman signed the new loan documents. (R. Doc. 1, at ¶98).

Despite the new agreement, Chrysler advised Gorman that it would not provide financing for non-suburban black customers regardless of their creditworthiness. (R. Doc. 249, at 2-3). And when the Dealerships refused to cooperate with Chrysler's discriminatory racial profiling of customers, Chrysler imposed financially ruinous penalties that forced Marquette out of business and substantially harmed Midlothian. (*Id.* at 3).

Ridge filed its Verified Complaint ("Complaint") against Chrysler on February 4, 2003, alleging claims for breach of contract, tortious interference with prospective business or economic advantage, violation of the Automobile Dealers' Day in Court Act, and violation of the Illinois Motor Vehicle Franchise Act, seeking compensatory and punitive damages. (R. Doc. 1).

On January 26, 2005, Chrysler filed two motions against Ridge and Gorman in the District Court seeking sanctions for alleged false statements and failure to produce and preserve evidence. (R. Doc. 180-181). On June 14, 2005, Magistrate Judge Arlander Keys submitted his Report and Recommendation ("Report") to the District Court recommending that the court dismiss Petitioners' Complaint with prejudice and grant Chrysler's motions for sanctions. (R. Doc. 249; Appendix C, 44a-95a). Following the submission of written briefs, the parties presented oral argument on Plaintiff's Objections to District Judge Virginia M. Kendall on February 24, 2006. (R. Doc. 280). On September 6, 2006, the district court issued a Memorandum Opinion and Order ("Opinion") (R. Doc. 282; Appendix B, 10a-43a),

adopting the Report in its entirety and dismissing the Complaint with prejudice as a sanction. (R. Doc. 282, at 26).

Petitioner pursued an appeal before the Seventh Circuit, and on February 20, 2008, the Seventh Circuit affirmed the decision of the District Court dismissing Petitioners' claims as a sanction. Finally, on March 17, 2008, the Seventh Circuit issued an Order denying Petitioners' Petition for Rehearing With Suggestion For Rehearing *En Banc*.

REASONS FOR GRANTING THE PETITION

This case presents significant issues relating to the appropriate standard to be applied in determining whether a discovery sanction should be imposed. The Seventh Circuit in this case imposed a "preponderance of the evidence" standard in determining whether the dismissal of a civil action as a sanction was appropriate, while a second panel of the Seventh Circuit issued a separate decision, two days thereafter, in the case styled *Ty, Inc. v. Softbelly's, Inc.*, 517 F.3d 494 (7th Cir. 2008), applying the more stringent "clear and convincing evidence" standard in determining whether a discovery sanction was appropriate.

Further, the Seventh Circuit's decision in *Ridge* expressly rejects the Seventh Circuit's previous precedent governing the applicable standard governing a sanction, as set forth in *Maynard v. Nygren*, 332 F.3d 462 (7th Cir. 2003), although two days later, a different Seventh Circuit panel embraced and followed this standard in *Ty, Inc. v. Softbelly's, Inc.*, 517 F.3d 494 (7th Cir. 2008).

Even more troubling than the irreconcilable conflict among the Seventh Circuit decisions addressing the issue, is the conflict between the Seventh Circuit's decision in this case and the decisions of five (5) of the other Circuits. The First, Second, Third, Eighth and D.C. Circuits have determined that when reviewing a sanction such as dismissal of a lawsuit, the appropriate standard of proof is clear and convincing. Certain panels of the Seventh Circuit have rejected this standard of proof, instead adopting the significantly lesser standard of the preponderance of the evidence.

This split of authority reflects diametrically opposed interpretations of the appropriate standard to apply in assessing a discovery sanction. With regard to the issue presented, whether a discovery sanction is appropriate is not governed by a single substantive legal consideration, but by the propriety of venue in a Court of the Seventh, First, Second, Third, Eighth or D.C. Circuits as well as within the Seventh Circuit, the fortuity of the panel to whom the case is assigned. In other words, geographic and temporal happenstance, rather than a consistently applied rule of law, informed by reasoned legal analysis and principles of fairness and justice, controls the question of whether a discovery sanction will be imposed. Final binding resolution of the issue by this Court is the only manner in which this manifestly unacceptable situation may be rectified.

In addition, absent review and reversal by this Court, the incorrect determination by the Seventh Circuit of the standard applied in imposing a discovery sanction will lend further confusion to an already convoluted legal analysis. Accordingly, review by this

Court is also necessary to clarify the propriety of the imposition of discovery sanctions in similar circumstances.

I. THE SEVENTH CIRCUIT'S INCORRECT DETERMINATION THAT THE STANDARD TO BE USED IN ASSESSING A DISCOVERY SANCTION IS THE PREPONDERANCE OF THE EVIDENCE, RATHER THAN CLEAR AND CONVINCING EVIDENCE, CONFLICTS WITH TWO OTHER DECISIONS OF THE SEVENTH CIRCUIT AS WELL AS DECISIONS OF THE FIRST, SECOND, THIRD, EIGHTH AND D.C. CIRCUITS ON THE SAME ISSUE.

A. A Conflict Exists Between The Standard Imposed By The Seventh Circuit In *Ridge* And The Standard Imposed By The First, Second, Third, Eighth and D.C. Circuits.

In several decisions issued by the First, Second, Third, Eighth and the D.C. Circuits, the respective courts found that dismissal of a case as a sanction must be supported by clear and convincing evidence, a heightened standard, as opposed to the preponderance of the evidence standard applied by the Seventh Circuit in *Ridge*.

In *Aoude v. Mobil Oil Corporation*, 892 F.2d 1115 (1st Cir. 1989), the First Circuit reviewed the dismissal of a complaint resulting from a purported "fraud on the court". The First Circuit found that dismissal of an action resulting from a fraud on the court must be

proven "clearly and convincingly" and that "because dismissal sounds the death knell of the lawsuit, district courts must reserve such strong medicine for instances where the defaulting party's misconduct is correspondingly egregious." *Aoude*, 892 F.2d at 1118 (internal citations omitted). The Court went on to state that dismissal "is an extreme remedy, and should not lightly be engaged." *Id.*

Similarly, the Second Circuit in *Mickle v. Morin*, 297 F.3d 114, 125-126 (2nd Cir. 2002), stated that "an award of sanctions under the court's inherent power must be based on clear evidence and must be accompanied by a 'high degree of specificity in the factual findings . . . .'" After reviewing the district court record, the Second Circuit vacated the order dismissing the action as a sanction and remanded the case for new trial.

The Eighth Circuit also addressed the issue of fraud on the court and stated, "[a] finding of fraud on the court is justified only by the most egregious misconduct directed to the court itself . . . and must be supported by clear, unequivocal and convincing evidence." *Pfizer, Inc. v. International Rectified Corp, et al.*, 538 F.3d 180, 195 (8th Cir. 1976). The court in *Pfizer* reversed a district court's grant of summary judgment as a sanction for withholding documents in discovery.

Finally, in *Shepherd v. American Broadcasting Companies, Inc.*, 62 F.3d 1469 (D.C. Cir. 1995), the D.C. Circuit was presented with an appeal from an order entering a default judgment against the defendant for non-compliance with discovery orders. In its opinion, the D.C. Circuit specifically addressed Federal Rule of Civil

Procedure 37 stating, "This rule permits the court to use such orders as are just to sanction a party that fails to obey an order to provide or permit discovery." *Id.*, at 1474 (internal citations omitted). The Court went on to conclude that a "heightened standard of proof" is a necessary prerequisite to the imposition of a dismissal sanction, stating:

> Because of the fundamental importance of trying cases on their merits, and, . . . because other sanctions can both deter and correct litigation misconduct when proven by only a preponderance of the evidence, the social disutility of granting a trial on the merits to a party guilty of litigation misconduct is less than the social disutility of denying a trial to a party innocent of such misconduct.

Id. at 1476. The Court found that misconduct that warrants dismissal as a sanction must be proven by a standard of proof higher than preponderance of the evidence, namely, clear and convincing evidence, and that this level of proof is "particularly appropriate because most inherent power sanctions, including default judgments are inherently punitive." *Id.* at 1476.

The Seventh Circuit's decision in this case constitutes a clear departure by the Seventh Circuit from the higher "clear and convincing" standard of proof embraced by the other Circuits. The Seventh Circuit's reliance on the lesser "preponderance of the evidence" standard establishes an irreconcilable split of authority amongst the circuits that requires review by this Court to resolve the confusion and to provide clear and

definitive direction as to which standard is appropriate. Without intervention by this Court, parties will be left with significantly different results in similar circumstances resolved not on the merits of their claims but on geographic fortuity.

B. The Seventh Circuit's Application Of A Preponderance Of The Evidence Standard Of Proof Required To Impose Sanctions In *Ridge* Conflicts With Other Decisions Of The Seventh Circuit Applying A Clear and Convincing Standard of Proof To The Decision To Impose Sanctions.

Both *Ridge* and *Ty* are cases in which a party was severely sanctioned. In *Ridge*, Petitioners' case was dismissed as a sanction principally because Petitioners' CEO, Gerald Gorman ("Gorman"), was perceived to have deceived the trial court.[2] *Ridge*, 516 F.3d at 624-625. In *Ty*, the plaintiff prevailed at trial, but because the trial court determined that Ty had tampered with a prospective opposition witness, it held that forfeiture of the jury's award of $713,000 in damages to Ty was the appropriate sanction. *Ty*, 517 F.3d at 496.

The common issue addressed by the Court in both *Ridge* and *Ty* was the appropriate evidentiary standard governing proof of misconduct necessary to support the

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[2] Because the sanctions imposed in this case arise from the Seventh Circuit's conclusion that Gorman had failed to cooperate in the discovery process and also had deceived the trial court, *Ridge* implicates both Rule 37 and the court's inherent authority to sanction a litigant, even though the Seventh Circuit was silent on this point.

imposition of a discovery sanction on a party for the misconduct. Notwithstanding an earlier Seventh Circuit opinion in *Maynard v. Nygren*, 332 F.3d 462 (7th Cir. 2003), which held that "considering the severe and punitive nature of dismissal as a discovery sanction, a court must have clear and convincing evidence of willfulness, bad faith or fault before dismissing a case" (*id.* at 468), the *Ridge* panel, concluded that the standard required to support dismissal as a sanction is the preponderance of the evidence standard. In reaching this conclusion, the Seventh Circuit cited *Grogan v. Garner*, 498 U.S. 279 (1991), and *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983), for the proposition that "heightened burdens of proof do not apply in civil cases unless a statute or the constitution so requires." *Id.* That statement, however, fails to acknowledge this Court's instruction in *Herman* that "[w]here congress has not prescribed the appropriate standard of proof and the constitution does not dictate a particular standard, we must prescribe one." *Herman*, 459 U.S. at 389.

Following that instruction, this Court's analysis in *Herman* led it to conclude that a preponderance of the evidence standard applies in Section 10(b) securities fraud actions because "[t]he interests of defendants in a securities case do not differ qualitatively from the interests of defendants sued for violations of other federal statues such as the antitrust or civil rights laws, for which proof by a preponderance of the evidence suffices." *Id.* at 390. This Court thus declined "to depart from the preponderance-of-the-evidence standard generally applicable in civil actions." *Id.*

Eight years later, in *Grogan v. Garner*, 498 U.S. 279 (1991), this Court once again determined the applicable standard in a matter wherein neither Congress nor the Constitution prescribed one. There, the issue was what standard applied to reach a finding of nondischargeability of a debt under Section 523 of the Bankruptcy Code given that the statute itself was silent on the issue. This Court followed *Herman*'s lead in prescribing the appropriate standard where neither Congress nor the Constitution did, holding that "[b]ecause the preponderance-of-the evidence standard results in a roughly equal allocation of the risk of error between litigants, we presume that this standard is applicable in civil actions between private litigants unless 'particularly important individual interests or rights are at stake.'" *Grogan*, 498 U.S. at 286.

Importantly, the Seventh Circuit in *Maynard* employed the analysis of the individual interests or rights at stake articulated by this court in *Herman* and *Grogan* and concluded that, "considering the severe and punitive nature of dismissal as a discovery sanction, a court must have clear and convincing evidence of willfulness, bad faith or fault before dismissing a case."[3] *Maynard*, 332 F.3d at 468. In so doing, the Court looked at cases from other circuits that reached the same conclusion. *Id.* (citing *Shepard v. American*

[3] Although the *Maynard* Court's analysis focused primarily on imposition of sanctions under Rule 37, that Court also addressed a court's inherent authority to impose sanctions, concluding that inherent authority sanctions, like Rule 37 sanctions, must be supported by a finding of willfulness. *Maynard*, 332 F.3d at 470. Consequently, the discussion herein applies equally to both species of sanctions.

Broadcasting Companies, Inc., 62 F.3d 1469 (D.C. Cir. 1995); *Aoude v. Mobil Oil Corp.*, 892 F.2d 1115 (1st Cir. 1989); *Pfizer, Inc. v. Int'l Rectifier Corp.*, 538 F.2d 180 (8th Cir. 1976); and *Scholastic, Inc. v. Stouffer*, 21 F. Supp. 2d 425 (S.D.N.Y. 2002)). In *Maynard*, the Seventh Circuit noted:

> [t]his holding brings the evidentiary standard applicable here into line with the standard applicable to justify dismissal for delay, contumacious conduct or failed sanctions. In all circumstances, to justify dismissal as a sanction, there must be clear and convincing evidence.

Maynard, 332 F.3d 469, n.3.[4]

In *Ridge*, the Seventh Circuit panel's reference to *Grogan* and *Herman* as support for the conclusion that the appropriate standard when a court is considering dismissal as a sanction is preponderance of the evidence ignores *Herman*'s and *Grogan*'s fact-specific analysis balancing the relative interests of the parties. Inexplicably, that panel summarily rejected *Maynard* as stating the appropriate standard, and went on to embrace a different standard than that approved in Maynard.

The Seventh Circuit in *Ty*, however, acknowledged that *Maynard* is "[t]he principal case in this circuit"

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[4] The Seventh Circuit in *Wade v. Soo Line Railroad Corp.*, 500 F.3d 559 (7th Cir. 2007), questioned whether *Maynard* should be overruled based on this Court's decisions in *Grogan* and *Herman*, but declined to do so.

stating the appropriate standard. However, because it viewed *Maynard* as involving Rule 37 violations and not a court's inherent authority to sanction misconduct,[5] the *Ty* Court did not cite *Maynard* for the appropriate standard. Instead, following the *Grogan/Herman* fact-specific analysis, the Seventh Circuit in *Ty* pointed to the cases cited in *Maynard* for the proposition that "in the absence of a statute or rule, the exercise of judicial authority should be governed by traditional common law or equitable principles, such as the familiar principle that fraud must be proved by clear and convincing evidence." *Ty*, 517 F.3d at 499.

The Seventh Circuit in *Ty* also concluded that regardless of the standard applicable in that case, the constitution "imposes (in the Eighth Amendment's cruel and unusual punishments clause) limitations on the severity of punishment, so the permissible level of sanctions for misconduct in litigation, except when prescribed by statute or rule, is, even when there is no heightened burden of proof, limited by notions of proportionality." *Ty*, 517 F.3d at 499.

C. The Seventh Circuit's Decision In *Ridge* Disregards The Accepted Analysis Required To Ensure That The Sanction Imposed Is Proportional To The Wrongful Conduct.

A manifest conflict exists between the Seventh Circuit's decisions in *Ridge* and *Ty* for the additional reason that, in *Ridge*, the Seventh Circuit disregarded the concept of proportionality. *Ty*, citing to *Allen v.*

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[5] See note 2, *supra*.

Chicago Transit Authority, 317 F.3d 696, 703 (7th Cir. 2003), among other cases, concluded that imposition of a sanction that amounted to nine times the amount necessary to compensate the victim was too harsh. *Ty*, 517 F.3d at 499. *Allen* is particularly instructive here because in that case, as in the present case, the issue was whether dismissal of a party's case was an appropriate sanction. In *Allen*, after concluding that one of the plaintiffs, Earnest Leonard, had perjured himself during his deposition, the district court ordered Leonard to pay the defendant $4,000 in ten installments of $400. *Allen*, 317 F.2d at 702. Leonard was late in making the first payment, which resulted in a defense motion to dismiss his suit as a sanction. *Id.* The motion was denied after he made the payment. By the time the case reached the Court of Appeals, however, Leonard was $1,800 in arrears. *Id.* The defendant thus asked the Seventh Circuit to dismiss his appeal as a sanction. *Id.*

Although the Seventh Circuit affirmed dismissal of Leonard's claims on their merits, it noted that dismissal as a sanction for perjury under the facts before it might have been too harsh. *Allen*, 317 F.3d at 702-703. Facts a court should consider under such circumstances include the conduct of the opposing party ("suppose the opposing litigant had perjured himself as well") and whether the perjury affected the course of the litigation. *Id.*

The Seventh Circuit in *Ridge*, however, took none of *Allen*'s proportionality factors into account and instead, citing to *Ball v. Chicago*, 2 F.3d 752 (7th Cir. 1993), accepted the "facts" as set out by the magistrate judge and adopted by the district court without reference to

the countervailing evidence in the record,[6] and concluded that Gorman had "deceiv[ed] Judge Andersen to obtain an order worth at least $500,000 to the dealerships." *Ridge*, 516 F.3d at 626. The Court thus affirmed dismissal of Petitioners' claims.

Consideration of whether the "punishment meets the crime" also ensures that the sanction imposed is consistent with the need for courts to exercise restraint in dismissing cases for bad faith conduct. As this Court has explained, because such "powers are shielded from direct democratic controls, they must be exercised with restraint and discretion." *Roadway Express, Inc. v. Piper*, 447 U.S. 752, 764 (1980). Dismissal on such a reduced standard of proof is also inconsistent with our judicial system's strong presumption in favor of adjudications on the merits. *Forman v. Davis*, 371 U.S. 178, 181-82 (1962); 5B Charles A. Wright & Arthur R. Miller, FEDERAL PRACTICE & PROCEDURE: CIVIL 3rd § 1357, at 599 & n.67 (3rd ed. 1969).

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[6] The *Ridge* panel plainly stated that "[t]he facts we are reciting come from Magistrate Judge Keys's findings, which District Judge Kendall approved after the case was transferred to her." *Ridge*, 516 F.3d at 624.

II. THE SEVENTH CIRCUIT'S TREND TOWARDS DISMISSING CASES AS A SANCTION, RATHER THAN ENTERING A LESSER SANCTION AND ALLOWING THE CASE TO PROCEED ON THE MERITS, PRESENTS AN IMPORTANT FEDERAL QUESTION ON THE INTERPRETATION OF THE FEDERAL RULES OF CIVIL PROCEDURE.

In recent cases such as *Ridge* and *Wade*, discussed *supra*, the Seventh Circuit has affirmed a sanction against a plaintiff that has resulted in the dismissal of a plaintiff's claims. These cases effectively result in defendants using the Federal Rules of Civil Procedure as well as the court's inherent power to act as a bar to a suit on the merits in order to circumvent the judicial process, and it is becoming more and more frequently used as a defense tactic. This defense tactic is successful in that it precludes a party from going to trial on the merits, but also results in a much more serious break down of a constitutionally enriched right – adjudication by a jury of claims on their merits.

There is no question that a court must possess a certain degree of authority to police its own docket to ensure that no party is engaging in an abuse of the judicial process. The principle has best been set forth by this Court in *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43 (1991):

> Courts of justice are universally acknowledged to be vested, by their very creation, with power to impose silence, respect, and decorum, in their presence and

> submission to their lawful mandates. These powers are governed not by rule or statute but by the control necessarily vested in courts to manage their own affairs so as to achieve the orderly and expeditious disposition of cases.

However, as set forth below these powers are limited in certain respects.

Rule 37 of the Federal Rules of Civil Procedure grants a court the power to dismiss a case as a sanction for non-compliance with a discovery order. In *Societe Internationale Pour Participations Industrielles Et Commerciales, S.A. v. Rogers*, 357 U.S. 197, 207 (D.C. 1958), this Court stated, "whether a court has power to dismiss a complaint because of noncompliance with a production order depends exclusively upon Rule 37." This Court then reviewed the sanction imposed and stated, "[t]he provisions of Rule 37 which are here involved must be read in light of the provisions of the Fifth Amendment that no person shall be deprived of property without due process of law." *Id.* at 209. Further, this Court found that "there are constitutional limitations upon the power of courts, even in aid of their own valid processes, to dismiss an action without affording a party the opportunity for a hearing on the merits of his cause." *Id.*

Similarly, courts are vested with certain inherent powers that are used when rules alone do not provide courts with sufficient authority to protect their integrity and prevent abuses of the judicial process. It is well settled that a court may dismiss an action as a sanction.

See, Link v. Wabash Railroad Comp., 370 U.S. 626 (1962), and *Chambers v. NASCO, Inc.*, 501 U.S. 32 (1991). However, when faced with dismissal as a sanction, the court must balance "the judicial system's need for an effective tool to discourage and punish misconduct with its need for appropriate restraint in imposing inherent power sanctions." *Shepherd v. American Broadcasting Companies, Inc.*, 62 F.3d 1469, 1475 (D.C. Cir. 1995). Further, as this Court stated in *Chambers*, "because of their very potency, inherent powers must be exercised with restraint and discretion." *Chambers*, 501 U.S. at 44.

Furthermore, there is a presumption in our judicial system that a resolution of a matter on the merits is preferable to a resolution based on a mere technicality. See, *Foman v. Davis*, 371 U.S. 178, 181-182 (1962). Routinely resorting to the dismissal of a case as a sanction, rather than allowing them to be adjudged on their merits, is in direct contravention of the spirit and nature of our jury system. Allowing a party to come into court with a Motion for Sanctions resulting from, for example, a statement made at a deposition, devalues the idea of impeachment at a trial on the merits and removes from the province of a jury the ability to weigh a party's credibility. The jurisprudence embraced by the Seventh Circuit's decision in this and other cases involving dismissal as a sanction invites parties to attempt to end the proceedings without regard for the merits of the cause, and while it is imperative to retain the high standard of truth and to maintain the solemnity of court proceedings, these factors must be weighed carefully against a party's Fifth Amendment right to

present his case on the merits to a jury and to have that jury make a decision based on all of the evidence presented before it.

Here, at a minimum, Petitioners were entitled to an evidentiary hearing as to the issues raised by the Respondent before the District Court rendered its decision. This Court should accept this Petition to address the strained relationship between a dismissal of a party's claims as a discovery sanction and a party's right to bring his case to trial on the merits, as well as the potential misuse of the Federal Rules of Civil Procedure to deny a party his day in Court.

CONCLUSION

For the foregoing reasons, this petition for writ of *certiorari* should be granted.

Respectfully submitted,

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APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DECIDED FEBRUARY 20, 2008

IN THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 06-4140

RIDGE CHRYSLER JEEP, LLC, and SALES, INCORPORATED,

Plaintiffs-Appellants,

v.

DAIMLERCHRYSLER FINANCIAL SERVICES AMERICAS LLC,

Defendant-Appellee.

Appeal from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 03 C 760—**Virginia M. Kendall**, *Judge.*

ARGUED SEPTEMBER 21, 2007
DECIDED FEBRUARY 20, 2008

Before EASTERBROOK, *Chief Judge*, and KANNE and ROVNER, *Circuit Judges.*

EASTERBROOK, *Chief Judge.* Ridge Chrysler Jeep and Dodge of Midlothian were dealers in Chrysler's vehicles. It provided floor-plan financing and was entitled by contract to withdraw or limit financing if its position

became insecure. (We refer to "Chrysler," which before its spinoff into Chrysler LLC was a division of DaimlerChrysler. Financing was by DaimlerChrysler Financial Services, which survived the separation of Chrysler from Mercedes Benz.)

In 2002 Chrysler exercised its right to require the dealerships to pay up front for their inventory. They responded with this suit under the Automobile Dealers' Day in Court Act, 15 U.S.C. §§ 1221-25, accusing Chrysler of effectively ending the franchises without adequate cause. Chrysler replied that it remained willing to furnish whatever the dealerships could resell; if they could not pay in advance they were free to obtain capital from the many other firms that specialize in loans secured by inventory.

After Gerald Gorman, the CEO and principal owner of the two dealerships, represented that he had been unable to obtain third-party credit, District Judge Andersen entered an interlocutory order compelling Chrysler to continue to finance the inventory, provided that Gorman raise new capital to improve Chrysler's position. Once Gorman filed an affidavit verifying that he had secured $925,000, the district judge's order took effect. Despite Fed.R.Civ.P. 65(c), the judge did not require the dealerships to give an injunction bond or other security, and Chrysler neglected to take an appeal from that omission. It has had cause to regret both the district court's oversight and its own inaction. See *W.R. Grace & Co. v. Rubber Workers*, 461 U.S. 757, 770 n. 14, 103 S.Ct. 2177, 76 L.Ed.2d 298 (1983); *Mead Johnson &*

Co. v. Abbott Laboratories, 201 F.3d 883, 887-88, amended, 209 F.3d 1032 (7th Cir.2000).

Discovery then got under way. The case was complex, because the dealerships made claims under state law and also argued that Chrysler had discriminated by refusing to finance the purchases of non-suburban black customers. For its part, Chrysler filed counterclaims seeking repayment of outstanding loans. Discovery was sidetracked once Chrysler learned that Gorman had lied to Judge Andersen. The supposed $925,000 in new equity was in fact a $750,000 loan from Edward Vrdolyak, then the dealerships' lawyer in this suit. The loan was secured by some of Midlothian's inventory and so did not provide Chrysler with a cushion, as Gorman had represented. The other $175,000 appeared to represent Gorman's sale of his shares in firms unrelated to the dealerships. Changing some of Gorman's existing assets from stock to cash did nothing to improve Chrysler's security.

Chrysler sought to discover the dealerships' business records, many of which were on a computer. First plaintiffs denied having any such computer; then they said that they could not access it after the dealerships closed in late 2003; by the time Magistrate Judge Keys ordered the dealerships to comply, the computer had been repossessed and destroyed by its owner. Gorman had failed to copy the data for disclosure to Chrysler. (The facts we are reciting come from Magistrate Judge Keys's findings, which District Judge Kendall approved after the case was transferred to her.)

The magistrate judge also found that Gorman had lied about his efforts to obtain loans from sources other than Chrysler. Gorman assured Judge Andersen that he had made personal inquiries and found banks unwilling to lend because of the pending litigation; in a deposition, however, Gorman conceded that he had not tried to obtain floor-plan financing from anyone other than Chrysler until after the district court entered its order. (Whether Gorman's representations should have led to any relief, had they been true, is open to doubt. Suppose that no one other than Chrysler was willing to finance the dealerships' inventory at any plausible interest rate. That judgment of independent financiers would establish, not that Chrysler should be compelled to loan more, but that it had good business reasons for thinking itself insecure.)

Plaintiffs' verified complaint asserted that the allegations of racial discrimination by Chrysler could be established by contemporaneous notes that Gorman had maintained. During discovery plaintiffs were unable to produce these notes. Whether they never existed, or existed but were destroyed to prevent revelation of their contents, is unknown.

To top this off, Gorman used the time when Chrysler was an involuntary creditor to pay himself $1 million of a loan to the dealerships that was supposed to be subordinated to Chrysler's position. Thus the promised $925,000 in new capital (which actually was no more than $750,000) was offset by a loss of $1 million in old capital. Gorman's "explanation" for this is that he deemed the

subordination agreement to be invalid. He didn't tell Chrysler about this view, or his action based on it, until he had been caught. As far as we can see, Gorman has never attempted to establish that the subordination agreement *is* invalid; he treats his unilateral belief as sufficient to justify going back on his word to both Chrysler and Judge Andersen.

When the dealerships closed, they owed Chrysler $4 million, about $500,000 more than when this litigation began. The district court ordered the dealerships to pay that debt on Chrysler's counterclaim, and it dismissed the dealerships' claims as a sanction for misconduct during the course of the litigation. 2006 WL 2808158, 2006 U.S. Dist. LEXIS 63664 (N.D.Ill. Sept. 6, 2006). Only the dismissal for misconduct is at issue on this appeal. Whether Chrysler will be able to recover much of the money that the district court ordered it to loan the dealerships without the security required by Rule 65(c) is uncertain.

Findings of fact must stand unless clearly erroneous, and a district judge's decision that a party's misconduct is serious enough to justify dismissal with prejudice is reviewed for abuse of discretion. *National Hockey League v. Metropolitan Hockey Club, Inc.*, 427 U.S. 639, 96 S.Ct. 2778, 49 L.Ed.2d 747 (1976). The limited scope of appellate review puts the dealerships behind the eight ball. They try to lighten their load by arguing that there is a strong presumption against dismissal as a sanction, and that only "clear and convincing evidence" can support outright dismissal. Although one recent

opinion in this circuit uses a "clear and convincing evidence" standard, see *Maynard v. Nygren*, 332 F.3d 462, 468 (7th Cir.2003), we have observed more recently that *Maynard* failed to discuss *Grogan v. Garner*, 498 U.S. 279, 111 S.Ct. 654, 112 L.Ed.2d 755 (1991), and *Herman & MacLean v. Huddleston*, 459 U.S. 375, 103 S.Ct. 683, 74 L.Ed.2d 548 (1983), which hold that heightened burdens of proof do not apply in civil cases unless a statute or the Constitution so requires. See *Wade v. Soo Line R.R.*, 500 F.3d 559, 564 (7th Cir.2007). Neither a statute nor the Constitution requires an elevated burden for dismissal as a sanction, when the burden in the underlying suit is the preponderance of the evidence. But we need not decide today whether the time has come to overrule *Maynard*, as the district court's findings suffice on any standard.

The dealerships' appellate arguments are uniformly unconvincing. They lead with the contention that the loan from Vrdolyak was to Gorman personally, not to Midlothian. This is unhelpful if true, for Gorman assured Judge Andersen that he had raised new equity capital. His affidavit says, among other things, "The source of the capital investment was not a loan from a third party that would require payment from dealership assets." But that is false. The record contains a note showing Midlothian as the borrower and grantor of security in its inventory. Vrdolyak wrote his check to Midlothian, and the money was deposited to a corporate account. Gorman says that he and Vrdolyak later agreed orally that the money would be treated as an unsecured loan to Gorman, but Vrdolyak himself did not agree. In a

deposition, Vrdolyak testified that Midlothian is the obligor on the note and Gorman a guarantor. Faced with a conflict between the written word and Gorman's uncorroborated assertion, it can't be clearly erroneous for the judge to prefer the writings. Especially when Gorman's testimony was undermined by the fact that Midlothian paid Vrdolyak $10,000 a month after the loan was made. Gorman has no explanation for these payments other than the inference that the district judge drew—that they are debt service on a loan.

Now consider the question whether Gorman lied to Judge Andersen about his efforts to obtain floor-plan financing. Gorman conceded during his deposition that he did not try to obtain such credit until after Judge Andersen entered his interlocutory order. When the consequences of this statement—it confesses to perjury in the affidavit filed with Judge Andersen—became clear, Gorman filed another affidavit taking another tack. The district court didn't have to buy the latest story. Nor was the district court obliged to interpret a banker's equivocal statement that he "could have" met Gorman before the court entered interlocutory relief as proof that Gorman *did* ask for a loan then. The banker added that his institution was too small to finance the dealerships' inventory. Midlothian needed $10 million in credit, and this bank's lending limit was $1.85 million. Gorman did not tell Judge Andersen that his requests for credit had been turned down because he approached lenders without the requisite capacity. Making a request that is certain to be rejected, for reasons unrelated to the probability of repayment, is not a good-faith effort

to replace Chrysler's financing; Gorman might as well have asked one of his children for a loan. So even by Gorman's latest version his affidavit at the outset of this suit was misleading.

It is unnecessary to discuss any of the other aspects of Gorman's chicanery, though they too are supported by adequate findings.

As for the sanction: we have held that the penalty must be proportionate to the wrong, see *Ball v. Chicago*, 2 F.3d 752 (7th Cir.1993), but this does not assist the dealerships. The principal wrong identified by the district court—deceiving Judge Andersen to obtain an order worth at least $500,000 to the dealerships—show that this suit entails an abuse of the federal court's process. One who misuses litigation to obtain money to which he is not entitled is hardly in a position to insist that the court now proceed to address his legitimate claims, if any there are. Plaintiffs insist that the claims of racial discrimination are legitimate, but that is dubious. The complaint and appellate brief narrate repugnant events, but when the time came in discovery to produce the notes that supposedly recorded the discriminatory statements by Chrysler's employees, the notes were nowhere to be found. Plaintiffs have behaved like a pack of weasels and can't expect any part of their tale be believed. Anyway, discrimination against would-be purchasers of cars is actionable by the persons discriminated against. A suit by persons claiming to be the victims of discriminatory failure to make loans has been filed and settled. *Coburn v. DaimlerChrysler*

Services North America, LLC, 218 F.R.D. 607 (N.D.Ill.). The dealerships are only incidental losers (if discrimination occurred at all), and this suit need not be kept alive on that account.

AFFIRMED

A true Copy:

Teste:

_____

Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B — MEMORANDUM OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED SEPTEMBER 6, 2006

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

Case No. 03 C 760

Judge Virginia M. Kendall

RIDGE CHRYSLER JEEP, LLC, d/b/a MARQUETTE CHRYSLER JEEP, et al.,

Plaintiffs/Counterclaim Defendants,

v.

DAIMLERCHRYSLER SERVICES NORTH AMERICA LLC,

Defendant/Counterclaim Plaintiff,

v.

GERALD GORMAN and ELIZABETH GORMAN,

Counterdefendants.

MEMORANDUM OPINION AND ORDER

Facts & History

Two Dodge dealerships, Ridge Jeep of Midlothian, Illinois (hereafter "Midlothian") and Marquette Jeep of Chicago, Illinois (hereafter "Marquette" and together

with Midlothian, the "Dealerships"), filed a verified complaint on February 3, 2003 against DaimlerChrysler Services North America LLC (hereafter "Chrysler" or "Defendant"). *See* Verified Cmplt., Docket No. 1. The Dealerships alleged that Chrysler persisted in a "shocking corporate policy of blatant racial discrimination and redlining" by refusing to provide financing for African-American customers purchasing cars at the Dealerships. *Id.* at ¶¶ 1, 4. The Dealerships alleged violation of the Automobile Dealers' Day in Court Act, as well as state law violations of the Illinois Motor Vehicle Franchise Act, tortious interference with prospective business advantage, and breach of contract. On the same day, class action plaintiffs filed a related suit against Chrysler for discrimination in lending, *Coburn v. Daimler Chrysler Services North America*, 03 C 759. The *Coburn* matter was assigned to a different judge in this district. The attorneys representing the Dealerships in the matter before this Court also represented the *Coburn* plaintiffs.

Mr. Gerald Gorman (hereafter "Gorman") is the president and owner of both Dealerships. *See* Verified Cmplt. at Verification. Gorman purchased Marquette in 1999 and Midlothian in 2000. *Id.* at ¶¶ 15-16. The basis for the allegations set forth in the Verified Complaint are numerous conversations between Gorman and various Chrysler representatives, portions of which are set forth in quotes in the Verified Complaint. *See, e.g., id.* at ¶¶ 28-39, 59, 62, 73, 106. Gorman personally verified the facts included in the Verified Complaint. The attorneys representing the Dealerships also

represented Gorman (the Dealerships and Gorman together "Plaintiffs").

On March 24, 2003, Chrysler filed a verified Counterclaim against the Dealerships, and added Gorman and his wife, Elizabeth Gorman, as counterclaim defendants. *See* Verified Counterclaim, Docket No. 13. Chrysler alleged that Plaintiffs defaulted on the terms of the original loan and security agreements between Chrysler and Midlothian through misleading statements, incomplete records, and payments from Midlothian to Gorman personally. *Id.* at ¶ 36-45. Chrysler alleged that these defaults jeopardized Chrysler's first-priority security interest in Midlothian's collateral. Chrysler also alleged that Marquette made misleading representations to Chrysler over the course of several retail financing contracts between Marquette and Chrysler, which statements caused Chrysler to enter into agreements with Marquette and Marquette customers that it would not have entered but for the misrepresentations. *Id.* at ¶¶ 52-58. Chrysler sought replevin against Midlothian, damages as against the Gormans for their personal guarantees of the Midlothian loan documents, and damages for breach of contract against both Dealerships.

The Temporary Restraining Order

On April 4, 2003, the Dealerships filed an emergency request for a Temporary Restraining Order ("TRO") against Chrysler. The Dealerships alleged that starting in the spring and summer of 2002, Chrysler had refused

to finance vehicle purchases from the Dealerships. Motion for TRO, Docket No. 23 at 5-6. By September 2002, Chrysler had ceased all vehicle financing for the Dealership and started audits of the Dealerships' financials. *Id.* at 6-7. The TRO request also alleged that by December 2002, after completing the audits, Chrysler threatened to stop all pending vehicle orders unless Gorman infused capital into the Dealerships and signed a release of claims against Chrysler, which Gorman refused to sign. *Id.* at 8-9. The TRO request alleged that by early 2003, Chrysler retaliated by restricting factory orders, terminating lines of credit and sending notice of repossession of the floor plan. *Id.* at 10. The Dealerships requested a TRO to reinstate the lines of credit, lift the factory order restrictions, and cease the floor plan repossession. The Dealerships alleged that without the TRO, they would be "forced out of business within days." *Id.* at 14.

On April 11, 2003, the Court granted a stipulated TRO, but only after Plaintiffs met certain conditions set by the Court. Gorman testified via supporting affidavit, filed with Plaintiffs' April 9, 2003 reply brief in support of the TRO, that he had: (i) tried to obtain alternate financing, but had been unable to due so due to the pending litigation, and (ii) put $925,000 of personal, unencumbered funds back into the dealership as working capital. *See* Affidavit of Gerald Gorman, April 9, 2003 at ¶¶ 2, 12, Docket No. 29. Gorman's affidavit specifically stated that the $925,000 "was an investment of personal money and is wholly unencumbered" and that the investment funds came from "sale of stock

certificates and a direct investment from a long time business associate." *Id.* at ¶ 2. The Court commented during the hearings on the TRO that the equity infusion was "essential" because the Court did not believe that "Chrysler Financial should be put in a position where it is in effect writing blank checks for Midlothian and does not have complete assurance that its position is not going to erode if it continues to be a floor plan lender." Tr. of April 8, 2003 Hearing at 16-18, Ex. C to Pltf.'s Objections to June 14, 2005 Ruling, Docket No. 262.

The Court granted a Stipulated Order on April 11, 2003 which, among other provisions, committed Chrysler to restore Midlothian's floor-plan financing for 180 days. The stipulated order stated, "Midlothian represents and warrants that a $925,000 equity capital infusion has been made, which is unencumbered and not to [sic] subject to repayment by Midlothian to the investment source." April 11, 2003 Stipulated Order at ¶ 9, Docket No. 80. Kevin Spivey, Senior Dealer Credit Manager of Chrysler, testified that Chrysler suffered losses of at least $585,464 as a result of the requirements placed on Chrylser by the April 11, 2003 Stipulated TRO. Spivey Aff., Sanctions Ex. S1 at ¶10.[1]

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1. As discussed below, Chrysler filed two motions for sanctions prompting this opinion. Chrysler filed one set of supporting exhibits for both motions. The two-volume filing, titled "Original Exhibits to Defendant's Motions for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for False Statements to the Court and for Failure to Produce and Preserve Evidence" is referenced hereafter as "Sanctions Ex. __." Exhibits to the False Statements motion are lettered; Exhibits to the Failure to Produce & Preserve Evidence motion are numbered.

Appendix B

Discovery

After granting the stipulated TRO, the Court referred all discovery matters to the Magistrate Judge. Discovery proceeded, with regular motions to compel, from April 2003 through December 2004. During the discovery period, the Magistrate Judge granted a motion by Chrysler for monetary sanctions against the Dealerships because Plaintiffs caused the delay by failing to comply with damages discovery requests. *See* Docket No. 139.

The Disqualification

In December 2003, on motion from Chrysler, the Magistrate Judge recommended that the Court disqualify the lead attorney for Plaintiffs, Edward Vrdolyak. *See* Report and Recommendation of December 2, 2003, Docket No. 102. Vrdolyak had already been disqualified by the judge handling the *Coburn* matter due to communications between Vrdolyak and a potential *Coburn* plaintiff whom Vrdolyak knew was an employee in the general counsel's office of Chrysler. *Id.* at 5-7. The Magistrate Judge agreed that disqualification would be appropriate in this matter as well, because the potential *Coburn* plaintiff by virtue of her position at Chrysler had access to confidential materials concerning this litigation, and Vrdolyak could have received confidential information about this matter through contact with her. *Id.* at 13-14.[2]

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2. The Court adopted the recommendation of the Magistrate Judge to disqualify Vrdolyak on September 30, 2004. *See* Docket No. 135.

As an additional and supplemental reason for disqualification, the Magistrate Judge noted that Vrdolyak revealed during his deposition that he had signed a $2.5 million note securing financing for Gorman's business operations, and that Vrdolyak received $10,000 per month from Gorman without explanation. *Id.* at 18-19.

On March 2, 2004, Chrysler moved to compel discovery from Vrdolyak concerning an alleged loan of $750,000 made from Vrdolyak to Gorman, which loan formed the majority of the $925,000 capital infusion into Midlothian used to fulfill the Court's requirement for the April 2003 TRO. *See* Docket No. 115. The Magistrate Judge granted Chrysler's motion to compel discovery about the loan. *See* Docket No. 122. Discovery on the loan revealed that Vrdolyak was the "business associate" referenced in Gorman's April 9, 2003 affidavit.

The Motions for Sanctions

In October 2004, the Dealerships filed a partial motion for summary judgment, which the Court took under advisement. *See* Docket Nos. 136, 151. On January 12, 2005, the Magistrate terminated his appointment because discovery matters had closed. *See* Docket No. 171.

On January 26, 2005, Defendant moved for sanctions against Plaintiff via two motions: one for false statements by Gorman in connection with the April 2003 TRO, and a second for deliberate efforts by Plaintiffs to conceal

discoverable material. *See* Docket Nos. 180-182.[3] The Court entered an order on February 9, 2005 reopening the referral to the Magistrate, who set a briefing schedule on the sanctions motions. *See* Docket No. 192-93.

Chrysler raised five separate issues of allegedly inappropriate conduct that it believed merited sanctions:

> (i) false testimony by Gorman in his affidavit of April 9, 2003, regarding the source of a $750,000 equity infusion;
>
> (ii) false testimony by Gorman in the affidavit of April 9, 2003 regarding Gorman's attempts to obtain alternate financing to that provided by Chrysler;
>
> (iii) false testimony by Gorman in the affidavit of April 9, 2003 and in deposition testimony concerning the Subordination Agreement between Midlothian, Gorman, and Chrysler;
>
> (iv) willful (or at least grossly negligent) failure to turn over to Chrysler a computer containing materially relevant data from Midlothian that could not be obtained elsewhere, as well as other missing financial data from the Dealerships; and

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3. Defendant also moved by separate motion for summary judgment on all counts of the complaint. *See* Docket Nos. 183-185. The Court has not ruled on this motion.

(v) "missing notes" — handwritten notes by Gorman — that formed the basis of the Verified Complaint.

Chrysler requested that the Court dismiss the Dealerships' complaint or, in the alternative, fine the Dealerships and Gorman, and give adverse instructions to the jury during the trial concerning the impact of the inappropriate conduct.

1. *Gorman's Affidavit Testimony regarding the $925,000 Capital Infusion*

During the hearings on the TRO in April 2003, the Court expressed concern that if the Court granted the TRO request, Chrysler would be forced to continue to finance a business that it alleged would lose money. Therefore, at the hearing on April 8, 2003, the Court clarified that Gorman would have to guarantee that additional equity had been placed into the Dealerships that would protect Chrysler from further losses. *See* April 8, 2003 Tr., Sanctions Ex. C at 16-17. Gorman swore in an affidavit dated April 9, 2003 that he had obtained $925,000 in late 2002 as additional, unencumbered equity for the Dealerships. According to the affidavit, the sources of the investment were "monies obtained from the sale of stock certificates and a direct investment from a long time business associate." *See* April 9, 2003 Aff. at ¶ 2.

As came to be revealed in late 2004, after Chrysler motioned to compel discovery and testimony from

Vrdolyak, the "personal loan from a business associate" was a check for $750,000 to Midlothian (not Gorman) from Vrdolyak, who at the time of the loan was lead counsel for Plaintiffs. Vrdolyak Dep., Sanctions Ex. V, at 96. Additionally, the evidence suggested that the "personal loan" was secured by the assets of Midlothian. Mr. Vrdolyak and Gorman signed a written contract in December 2002 for the $750,000, granting to Vrdolyak "as collateral used cars subject to all UCC filings" and "ownership documents concerning [Midlothian] and companies . . ." *Id.* at 100-104. Although both men testified under oath that their "personal understanding" of this agreement changed a few days later, Vrdolyak also testified at his deposition that he considered the money to be a loan to Midlothian that would be repaid (by either Midlothian or by Gorman personally.) *Id.* at 107-112, 124-26. The $750,000 check was made payable to "Midlothian Dodge" and stated in the memo line that it was a "loan." Gorman Dep., Sanctions Ex. G, at 2166. The bank records showed that the check was deposited into the Midlothian account. *Id.* Although Vrdolyak testified that he considered the loan to be "interest-free," a review of Vrdolyak's finances showed that he had accepted routine payments from Midlothian accounts - not from Gorman personally. Vrdolyak Dep, Sanctions Ex. V, at 127-36; Gorman Dep., Sanctions Ex. G, at 2206-12.

In addition to the $750,000, the "sale of stock certificates" forming the remaining $175,000 of the equity infusion could not be traced clearly to Gorman's personal assets as opposed to Midlothian's assets. At

the time of the purchase of the stock, Gorman withdrew money for the purchase from a Midlothian account, and recorded the cash withdrawal as a transfer between Midlothian accounts rather than a stock purchase. Gorman Dep., Sanction Ex. G, at 2094-2101. The stock was issued to Gorman and his wife, not to Midlothian. Hogan Dep., Sanctions Ex. H, at 142-144; Gorman Dep., Sanctions Ex. G, at 2078-2079. Gorman claimed that he transferred the stock to Midlothian at some point prior to the sale, but Gorman remained the owner of record even after the stock had been sold, and still listed the stock as a personal asset when applying for loans in February 2003. Gorman Dep., Sanctions Ex. G, at 2553-2556.

Chrysler alleges that both the $750,000 and the $175,000 were assets of Midlothian rather than Gorman's personal assets, and that the $750,000 portion of the equity financing was encumbered by the assets of Midlothian. According to Chrysler, all of these facts indicate that the April 9, 2003 Affidavit contains false statements, and that the false statements influenced the Court to grant the TRO to the Dealerships to Chrysler's detriment.

2. *Gorman's Affidavit Testimony about Alternate Funding*

Gorman testified in his April 9, 2003 affidavit that he made two attempts to find alternate floor plan financing prior to seeking the TRO, but that banks would

not agree to financing due to the pending litigation with Chrysler. *See* April 9, 2003 Affidavit at ¶ 12. But, in his deposition months later, Gorman stated that he had sought financing *after* the TRO had been granted, not before. Gorman Dep., Sanctions Ex. G, at 2174; 2584-86. Additionally, a bank employee who spoke with Gorman about floor plan financing further testified that his banks did not reject Gorman due to the pending litigation at all, but rather due to the size of the financing he had requested. Hogan Dep. at 114-117. Chrysler alleges that these statements directly contradicted the testimony of Gorman in the April 9, 2003 affidavit.

3. *The Subordinated Note*

In 2000, prior to the lawsuit at issue here, Gorman and Midlothian executed a Subordination Agreement with Chrysler, whereby $4.5 million in debt owed by Midlothian to Gorman would be subordinated to the claims of Chrysler. Answer to Verified Counterclaim at ¶ 23. In the Verified Counterclaim, Chrysler alleged that Midlothian made payments toward the $4.5 million owed to Gorman in violation of the terms of the Subordination Agreement. Verified Counterclaim at ¶ 43. In the April 9, 2003 Affidavit, Gorman testified that the $4.5 million debt had been reduced by nearly $1 million. April 9, 2003 Aff. at ¶ 11, Docket No. 29. In their reply brief in support of the TRO, to which the Affidavit provided support, Gorman and Midlothian argued that the Subordination Agreement was a "sliding" note that allowed Gorman to remove money from Midlothian. Reply Brief at 5-6, Docket No. 28. But, during his deposition in 2004,

Gorman argued that the Subordination Agreement was an invalid document. Gorman Dep., Sanctions Ex. G, at 1969-78. Chrysler alleges that the deposition testimony, the Affidavit, and the Answer to the Verified Counterclaim are all inconsistent and indicate false statements by Gorman with respect to the treatment of the subordinated debt.

4. *The Missing Financial Data*

The Dealerships maintained their financial records and general balance sheet electronically, on a computer and accounting system rented from Reynolds & Reynolds, a data system vendor specializing in auto dealerships. Gorman Dep., Sanctions Ex. G, at 485-92. The data for Midlothian was maintained on a computer located at Midlothian. Temple Dep., Sanctions Ex. T-2, at 68-69. The Dealerships also maintained backup tapes of the information located on their computers in the event that something caused the computer data to be erased. Gilmartin Dep., Sanctions Ex. J-2, at 30-32. The Dealerships also allegedly printed reports of some portions of the balance sheet. Gorman Dep., Sanctions Ex. G, at 485.

Starting in May 2003, Chrysler issued discovery requests to the Dealerships to produce the balance sheet information in both paper and electronic form. The Dealerships responded that they would produce the relevant and non-privileged information they had in their possession. Sanctions Exs. 1 at ¶¶ 23-24; Ex. 2 at ¶ 35. The Dealerships produced some paper records,

but not a complete set of the financial records for the relevant periods. They produced most of Midlothian's monthly data from September 2000 through August 2003, Marquette's monthly information in paper form for 1999 and 2002, and backup tapes for Marquette for 1999. The Dealerships did not produce Marquette's monthly information in any form for 2000 and 2001, or most of the backup tapes, or the electronic balance sheet. Keller Expert Report, Sanctions Ex. K, at 3-6.

Starting in early 2004, Chrysler began to ask about the missing paper and electronic financial information. Chrysler's attorneys specifically requested the electronic version, stating that the "client's financial information — including their general ledgers — was stored on your clients' computers." Sanctions Ex. 3. Counsel for Plaintiffs responded that "all Reynolds & Reynolds material in the possession of the dealerships or owner have been produced." Sanctions Ex. 4. A few days later, counsel for Plaintiffs restated "as for financial records on hard drive or discs, my clients again have none." Sanctions Ex. 5. Counsel for Plaintiffs reiterated in correspondence in May 2004 that "the dealerships have not had access to the Reynolds & Reynolds system since [the dealerships] went out of business." Sanctions Ex. 7. Chrysler never received the data that had been missing since the initial productions in late 2003.

When Chrysler deposed Gorman in June 2004, Gorman testified that there was no computer at Midlothian as of the date of his deposition, and that he did not know the location of any hard drive. Gorman

Dep., Sanctions Ex. G, at 505. He testified that he had "checked every square foot" in the Midlothian building, but did not find anything else. *Id.* When Chrysler at last deposed Mr. Temple, the Dealerships' chief financial officer, he testified that Reynolds & Reynolds repossessed the physical computer from Midlothian's offices in October 2004. Temple Dep., Sanctions Ex. T-2, at 68-74. He also testified that he told counsel about the repossession shortly after it occurred. *Id.* at 74. Plaintiffs' counsel did not communicate to counsel for Chrysler that the computer had been repossessed in October 2004.

Chrysler alleges that the financial data from both Midlothian and Marquette contained in the computer would show that Plaintiffs engaged in inappropriate accounting practices that gradually dwindled the value of each of the Dealerships. This, Chrysler alleges, would show that any financial harm to the Dealerships came not from Chrysler's alleged discriminatory lending practices, but rather from the poor management of the Dealerships. Chrysler alleges that Gorman and the Dealerships wilfully withheld the Reynolds & Reynolds computer, containing the electronic financial data for Midlothian, and at least negligently withheld backup tapes and paper records, to the extent such records existed, for both Midlothian and Marquette.

5. *The Missing Notes*

In the Verified Complaint, the Dealerships allege that Chrysler employees made blatantly racist comments to Gorman during company meetings. Verified Cmplt. at ¶¶ 28-39. These allegations are framed as block quotes, rather than general allegations of fact. *Id.* Gorman verified the complaint, and alleged that these block quotes came from notes of several conversations between himself and certain employees of Chrysler. Gorman Dep., Sanctions Ex. G, at 1109-1110. Chrysler issued a discovery request for "all documents" that referred to meetings between Gorman and employees of the Dealerships and employees of Chrysler, and received some handwritten notes, but when asked to point to the racial slurs in those notes, Gorman could not find the quoted passages and suggested that there might have been additional notes that had been lost or given to his attorneys. *Id.* at 684-86, 690-94. Gorman then recanted this statement in a supplemental affidavit in March 2005.[4] Chrysler alleges that the missing notes improperly formed the basis of a Verified Complaint, when such notes may well have never existed.

The Magistrate Judge's June 14, 2005 Opinion

In his detailed, 48-page Report and Recommendation of June 14, 2005, the Magistrate Judge decided that the combination of evidence

4. The Supplemental Affidavit is attached to Plaintiff's Response to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence, Exhibit F. Docket No. 206.

presented by Chrysler constituted "clear and convincing evidence" that Gorman had made false statements and that Gorman and/or the Dealerships had concealed relevant discoverable material. The Magistrate Judge found that "a lesser sanction is inappropriate" and recommended dismissal with prejudice.

The Magistrate Judge found that three issues raised by Chrysler constituted "clear and convincing evidence" of either false statements or willful concealment of evidence: the statements in the April 9, 2003 affidavit concerning the $750,000 loan, and those concerning the attempts to obtain alternate financing, and the failure to turn over the Reynolds & Reynolds computer during discovery. The remaining factual issues — the $175,000 stock sale, the missing paper data from Midlothian and Marquette, the statements concerning the $4.5 million subordinated debt, and the missing notes — formed additional support for the Magistrate's decision that the case had been tainted with discovery violations and at least misleading statements throughout its course. Taken in total, and combined with the previous requests for sanctions by Chrysler, the Magistrate Judge found that dismissal with prejudice would be the only appropriate course of action in this case.

The Plaintiffs timely filed their objections to the Magistrate Judge's report in the summer and fall of 2005.[5] At the request of the Dealerships and Gorman, the Court held oral argument on the objections on February 24, 2006.

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5. The case was reassigned to this Court as part of the Court's initial docket on January 23, 2006. Docket No. 274.

Appendix B

Based on a review of the entire record and the Magistrate Judge's analysis, this Court adopts the Report and Recommendation of the Magistrate Judge and dismisses the case with prejudice.

Legal Standard

When considering the extreme sanction of dismissing a case with prejudice, the Court is mindful of the admonition that such a step "must be infrequently resorted to by district courts." *See Schilling v. Walworth County Park and Planning Commission*, 805 F.2d 272, 275 (7th Cir. 1986); *United States v. Golden Elevator, Inc.*, 27 F.3d 301, 303 (7th Cir. 1994). Recognizing that such a harsh sanction should only be used in "extreme situations," this Court reviewed the entire record of this matter to determine whether such "contumacious conduct" existed and "whether less drastic sanctions have proven unavailing." *See Webber v. Eye Corp.*, 721 F.2d 1067, 1069 (7th Cir. 1983). Also aware that the Court's discretion is narrowed when imposing such a harsh penalty, the Court has reviewed Plaintiff's conduct in relation to all aspects of the judicial process. *See Halaco Engineering Company v. Costle*, 843 F.2d 376, 379 (9th Cir. 1988).

Even recognizing the need for such restraint and review, "there are species of misconduct that place too high a burden . . . for a court to allow a case to continue." *Barnhill v. United States*, 11 F.3d 1360, 1368 (7th Cir. 1993). Both Rules 37 and 41 permit the Court to sanction a party for failure to comply with discovery orders if the

district court finds willfulness, bad faith, or fault, especially in circumstances where a pattern of noncompliance with the district court's orders has been established. *See e.g. Ladien v. Astrachan*, 128 F.3d 1051, 1056 n.5 (7th Cir. 1997) (plaintiff's failure to timely produce discovery, his ex parte communication with the court, and his impermissible contact with witnesses warranted dismissal with prejudice); *Newman v. Metro. Pier & Exhibition Auth.*, 962 F.2d 589, 590-91 (7th Cir. 1992) (plaintiff's failure to respond to interrogatories and refusal to be deposed warranted dismissal with prejudice).

When discovery non-compliance, however, is coupled with lies to both an adversary and the Court in order to gain an advantage in the litigation, the Court must step in and impose the ultimate sanction in order to preserve the integrity of the federal judicial system. The Magistrate Judge's Report and Recommendation documents such a pattern of deception on behalf of Mr. Gorman that has so tainted the litigation that the very allegations set forth in the Complaint can not be trusted as being valid.

The case began with serious allegations of discrimination which were supported by the alleged notes that were maintained by Gorman and which formed the basis of his charges against Chrysler. The Court, at the time of the Motion for Temporary Restraining Order, took those allegations to be true, as it was required to do. Relying on the verified complaint, and the seriousness of the allegations, the Court crafted

an agreed restraining order to maintain the status of the parties while the litigation ensued. But the Court recognized that Defendant could not be held financial hostage to Plaintiff if Defendant's counterclaims proved to be true — that the termination of the lines of credit was due to the quickly sinking financial condition of the dealerships and their theft of over $1 million to pay debts owed to Mr. Gorman. Relying on the statements of Mr. Gorman that he would infuse unencumbered capital into the operation in order to preserve Defendant's financial position, Judge Andersen granted the TRO. Meanwhile, Chrysler sought to prove its counterclaims by obtaining the financial records believed to support their claims that were stored on the computers maintained by Plaintiffs.

In the end, the Magistrate Judge's findings, which are thoroughly supported by the record, revealed that notes Gorman used to support the most inflammatory allegations in the Complaint either did not exist, were not preserved, or worse yet, were fabricated in the first place; the computers that could have supported Defendant's defense and counterclaims were concealed and then destroyed in spite of preservation notices and repeated requests by Defendant, and the TRO was entered due, in significant part, to the false statements of Mr. Gorman who lied about both the source and status of the funds that were infused into the dealerships. This intentional conduct on the part of Plaintiffs can not be tolerated in a court of law where judges rely on the sworn statements of witnesses to reach objective decisions on the merits.

Appendix B

False Statements

The Magistrate Judge correctly held that Mr. Gorman made two distinct misrepresentations. The first lie occurred in his April 9, 2003 affidavit when he stated that he personally made a $925,000 capital investment into the dealership which was unencumbered. As stated above, the unencumbered nature of the investment was critical to Judge Andersen's decision in granting the TRO. The evidence does not support Plaintiffs' version that the money from Mr. Vrdolyak was unencumbered because a written agreement between Vrdolyak and Gorman provided that the $750,000 loan to Midlothian would give Vrdolyak "as collateral used cars subject to all UCC filings as directed and controlled by First Suburban National Bank and its president" and ownership documents concerning the business and a "pro rata percentage of profits and losses." Vrdolyak confirmed in his deposition that the money was not a gift and that he expected it to be repaid. Gorman admitted that Midlothian's cash disbursements journal showed payments that were most likely payments made on the loan. The money was originally obtained by Vrdolyak who took out a loan from First Suburban National Bank and then turned over the money to the dealership. Both men intended that Vrdolyak would be repaid and the dealership was responsible for repaying the loan. This evidence clearly shows that the $750,000 was not a "direct investment from a long time business associate" but rather a loan secured by collateral — exactly the situation that the district court judge sought to avoid by requiring an unencumbered asset before entering the TRO.

Appendix B

The Magistrate Judge also correctly held that Mr. Gorman lied to the Court regarding whether he sought to obtain financing from banks prior to Chrysler placing Midlothian on financial hold. Mr. Gorman stated in his affidavit to Judge Andersen that he went to two different banks to try to take out loans to refinance the floor plan at Midlothian. This statement, of course, was critical to that court's review of the Plaintiff's motion for temporary restraining order. If Plaintiffs were unable to obtain any other financing except that from Defendant, in spite of their efforts to do so, the court would give Defendant's withdrawal of financing more weight due to its extreme impact on Plaintiffs than if other financing was available. This lie was made directly to the Court to gain a strategic and economic benefit for Plaintiffs during the litigation and resulted in the Court entering the judicial relief they sought. In truth, the Court relied on a misrepresentation in granting the relief requested; one which would have significantly altered the outcome of that relief, and one might reasonably conclude, such relief would not have been granted but for the misrepresentation.

These two misrepresentations, as set forth and supported by the record, resulted in Plaintiffs obtaining equitable relief to which they were not entitled and placed Defendant in an unfair financial position by placing it at risk of financial erosion. Therefore, the Magistrate Judge correctly held that lying in a formal proceeding warranted such a sanction, and this Court agrees. *See also ABF Freight System, Inc. v. NLRB*,

510 U.S. 317, 323 (1976) (False testimony in a formal proceeding is intolerable.).[6]

Failure to Produce and Preserve Evidence

Because the nature of Defendant's defense and its counterclaims required an analysis of the financial records of the dealerships, Defendant sought to have the dealerships' computers preserved and reviewed, as well as, other financial records including monthly accounting journals, schedules, and notes.

Once again, Mr. Gorman lied in his deposition. This time, he claimed that he had not seen the computers "lying around the store" and did not know where they were in June of 2004. Yet, the dealership's Chief Financial Officer, Shawn Temple, testified that the computers were repossessed by Reynolds and Reynolds about two months before he gave his deposition in

6. The Magistrate Judge correctly refrained from finding that Gorman misrepresented the nature of the $175,000 from Mr. Fitzgibbon and that Gorman lied regarding the $4.5 million subordinated note from Midlothian. The record is not as clearly established on these issues and therefore the Magistrate Judge correctly withheld using the statements as support for his Report and Recommendation that the conduct of Plaintiffs required the dismissal of this case. This exercise of restraint further weakens Plaintiffs' position at oral argument that the Magistrate Judge was biased against Vrdolyak and Plaintiffs. It demonstrates, instead, that the Magistrate Judge objectively weighed the evidence and only relied on those statements that clearly showed that Gorman had lied based on all of the evidence before him.

December of 2004 — which would mean that the computers were not repossessed until months after Gorman's testimony. The Magistrate Judge correctly held that Plaintiffs concealed the true nature of the location of the computers by stating in April 2004 that they did not have access to the computers. In truth, the computers were still on site. Arguably, and even giving Plaintiffs the benefit of their interpretation, their incomplete answer regarding lack of access was given to mislead Defendant into believing that the computers were not in existence. In truth, they should have informed Defendant that the computers were on site, that they were being repossessed by Reynolds within the near future, and that if Defendant wanted access to them it would need to seek access through Reynolds. This type of gamesmanship was employed to prevent Defendant from defending against Plaintiffs' allegations and from supporting its counterclaims and can not be condoned.

Aside from the original computers, computer back-up tapes and journals were also requested during discovery, neither of which were produced. As for the missing journals from the most relevant years of the dealership, 2000-2001, Mr. Gorman stated originally that they were turned over and then later that he had no idea where they were in spite of his efforts to find them. In spite of Defendant's clear efforts to both seek preservation of these items and then review of them, neither have been produced. The Magistrate Judge correctly concluded that the absence of these items reflects poorly upon the credibility of Plaintiffs and

correctly did not rely solely on their absence in reaching his conclusion that a pattern of discovery abuse had occurred in the matter.

The Magistrate Judge did, however, conclude that Mr. Gorman's "missing notes" played a significant role in his findings. These notes which were the documentation that allegedly supported Plaintiffs' position that a Chrylser representative used explicit racial slurs and expressed extreme racially discriminatory views at meetings with Gorman and Temple, formed the basis for the quoted allegations within the Complaint. In his deposition, Mr. Gorman stated that he took notes of his meetings with this Chrysler representative during which these inflammatory statements were made and that his notes reflected those meetings and those slurs. Yet, at deposition, he was unable to point to any place in his notes where such comments were documented let alone to indicate that any such meetings took place. This led to a six-month period of discovery during which time Defendant sought to locate the notes which Gorman first alleged he gave to his attorney, next that they were lost, and finally, that they may not have existed at all but rather were confused with a five-page written summary of the case. The Magistrate Judge correctly viewed Gorman's testimony in light of his other lies to the court, the missing computers and logs, and his delays in completing timely discovery and held that the answers regarding the notes were meant to mislead the Defendant.

Appendix B

Pattern of Behavior

Finally, the Magistrate Judge correctly reviewed the entire record before him and took into account his earlier Report and Recommendation (which was eventually adopted by the court) requiring the disqualification of Vrdolyak due to his complete lack of respect for Court orders and the judicial proceedings. At oral argument, Plaintiffs reiterated their concern that the Magistrate Judge was biased against Vrdolyak and that bias led to this ultimate recommendation for dismissal. A careful review of the entire record reveals no such bias. Rather, the Magistrate Judge frequently refrained from findings where the evidence could be interpreted in favor of Plaintiffs and never relied on that evidence in reaching his conclusions. His careful and meticulous examination of the record is supported by this Court's review of the same.

Lesser Sanctions are Not Sufficient

The decision to dismiss a case with prejudice for discovery abuses and false statements is not a decision the Court makes lightly. "[T]he careful exercise of judicial discretion requires that a district court consider less severe sanctions and explain, where not obvious, their inadequacy for promoting the interests of justice." *Schilling v. Walworth County Park & Planning Com'n*, 805 F.2d 272, 275 (7th Cir. 1986). Dismissal with prejudice is appropriate in limited circumstances, "when there is a clear record of delay or contumacious conduct, or when other less drastic sanctions have proven unavailing."

Webber, 721 F.2d 1067, 1069 (7th Cir. 1983). In the case of dismissal under Rule 37, a slightly different standard applies, and the sanction of dismissal is reserved for cases in which the offending party has demonstrated wilfulness, bad faith, or fault. *See Maynard v. Nygren (I)*, 332 F.3d 462, 468 (7th Cir. 2003) (addressing both dismissal for delay and dismissal for willfulness or bad faith); *see also Long v. Steepro*, 213 F.3d 983, 986 (7th Cir. 2000). Under both these standards for sanctioning, the violating conduct must be clear and convincing. *Maynard I*, 332 F.3d at 468 (remanding sanction of dismissal to district court for explanation of evidence supporting sanction of dismissal). The choice between dismissal and lesser sanctions is a product of weighing three main considerations: (i) prejudice to Defendant as a result of Plaintiffs' conduct, (ii) prejudice to the judicial system, and (iii) deterrence and punishment. *Schilling*, 805 F.2d at 275, *citing Shea v. Donohoe Constr. Co.*, 795 F.2d 1071 (D.C. Cir. 1986); *see also Larson*, 2005 WL 4652509 at *8.

The detailed findings of the Magistrate Judge establish clear and convincing violations by Plaintiffs with respect to the false statements in the April 2003 affidavit underlying the TRO and in the failure to turn over the essential records on the Reynolds & Reynolds computer. Chrysler has provided to the Court a multitude of exhibits supporting its contentions, including affidavits, deposition transcripts, and letters between counsel, with thorough examinations in its written submissions in support of sanctions. *Compare Maynard v. Nygren (II)*, 372 F.3d 890 (7th Cir. 2004)

(affirming after remand a sanction of dismissal after district court credited circumstantial evidence as clear and convincing evidence of untruthfulness).

This clear and convincing evidence reveals that the Plaintiff, Gorman, lied in an affidavit submitted to the court in order to gain a monetary and strategic advantage over Defendant; misled Defendant as to the existence and location of evidence (the computers) which resulted in that evidence not being available for Defendant's use in these proceedings; and either lost key pieces of evidence (notes of his conversations with Defendant's agent) or fabricated their existence in the first instance, in an effort to bolster his position before the court and to inflame the passions of the court and the public. Each of these abuses can not be remedied by a monetary fine because each has resulted in damage that can not be remedied.

In the case of the false affidavit, it was due to this lie, in significant part, that the Court entered an order requiring Defendant to continue to provide floor plan financing to Plaintiffs during the pendency of this action. That false representation was bolstered by another — that plaintiff had sought financing from two other sources but could not obtain it due to the pendency of the litigation. These false statements were made to weight the scale on Plaintiffs' behalf in order to convince the district court judge that it was imperative that Defendant continue its business relationship in spite of their vehement objection to do so over concerns that they would be pumping money into a sinking concern.

As a result of that extension of financing, Defendant has lost approximately $500,000 — a monetary loss that it expressly professed to the Court as a real possibility when they opposed the extension of financing to Plaintiffs. That money would not have been lost had the appropriate unencumbered asset been provided as part of the Court's order. Aside from the monetary loss, Defendant was placed in a position that required them to continue to do business with an entity and with individuals that it strongly believed had breached contractual obligations and had engaged in improper accounting practices and possible unethical conduct.

Second, the allegations of discriminatory intent that were proclaimed throughout the Complaint — allegations that were publicly disseminated — were used strategically before the district court to emphasize the seriousness of the charges. Those serious accusations had greater import due to the affirmation that they were direct statements from agents of Defendant and were documented at the time they were made. The quoted sections within the Complaint are extreme examples of discriminatory intent. Defendant rightfully sought the full disclosure of the notes in order to determine the veracity and seriousness of the accusations. When those notes were not produced and the testimony regarding their existence became so muddled that even their original existence is in question, Defendant was placed at an extreme disadvantage in attempting to defend against such serious and inflammatory allegations.

Appendix B

Third, the computers that were withheld from the defense could have supported Defendant's theory that the withdrawal of floor plan financing was due to the financial incompetence of Plaintiffs and not from discriminatory motivations. Defendant took all appropriate steps to preserve that evidence to support its defense and counterclaims, yet Plaintiffs either intentionally concealed their existence until they were destroyed or acted with such incompetence that they were eventually destroyed. Either way, this critical evidence is lost forever and now Defendant is left to reconstruct its theories from spotty records and incomplete books. A monetary sanction can not bring that evidence back to life.

There is no doubt that Chrysler has been prejudiced by the conduct of Plaintiffs throughout this case. The Court relied upon Gorman's affidavit to compel Chrysler to enter into a TRO that cost Chrysler in excess of half a million dollars. Chrysler has defended itself in this lawsuit for more than three years, and the discovery materials withheld by Plaintiffs are the key elements to Chrysler's defense to the claims alleged by Plaintiffs. *Compare Marrocco v. General Motors Corp.*, 966 F.2d 220 (finding that plaintiffs' "willful and unexcused violations" of a protective order resulting in the destruction of evidence "certainly qualify as contumacious conduct.")

As to the prejudice to the legal system from Plaintiffs' conduct, this case merits the harsh sanction of dismissal. The pattern of behavior exhibited by

Appendix B

Plaintiffs included at least one prior incident of being fined for their abuse which demonstrates that the monetary sanction had little or no impact on deterring them from acting in the inappropriate manner in which they did. The Magistrate Judge correctly identified the difficulties during discovery which led to his eventual order requiring Plaintiffs to reveal the source of the money presented as part of the April TRO. Plaintiffs did not willingly reveal Vrdolyak's role in the TRO money, requiring the Magistrate Judge to hold hearings to determine the source of that money. These are not the actions of truth-seeking individuals intent on having their day in court, but rather, sleight of hand tactics of manipulators seeking to use the federal court system to their own advantage. Plaintiffs' actions with respect to the discovery violations constitute *contumacious* violations, having continued for nearly two years despite repeated requests from counsel for the Defendant, initially polite, and then increasingly firm, as the records and information essential to Defendant's defense were not forthcoming. Even lacking prejudice to the non-offending party, a Court is entitled to say "enough is enough" in the face of flagrant violations by one party. *See Larson*, 2005 WL 4652509 at *9.

The Court notes also that the completed settlement of the class action plaintiffs in the *Coburn* case gives the Court comfort that the individual consumers who purchased vehicles from Midlothian and Marquette have been compensated. The allegations in the matter before this Court involve only the dealerships and Gorman; therefore, the decision to dismiss this case with prejudice

will not result in harm to those customers of the dealerships even if the conduct alleged in this suit occurred. That matter has been resolved and is not pending before this court.

Finally, the Court finds that punishment and deterrence of conduct like Plaintiffs' requires dismissal with prejudice rather than a lesser sanction. Plaintiffs request in their motion to reconsider the Magistrate Judge's ruling that the Court consider lesser sanctions, such as fines against Plaintiffs or adverse jury instructions at trial. But the harm to Chrysler in this case cannot be cured by monetary sanctions. This is not a matter of missed status calls or late filings, causing inconvenience and delay to Chrysler and the Court. This is a matter of *lost or concealed evidence* — essential evidence — that directly flows from Plaintiffs' conduct, and a TRO forcing Chrysler to continue to do business with Plaintiffs based on Plaintiffs' untruthful statements. These violations cannot be cured through fines, and adverse jury instructions cannot replace lost evidence essential to a case.

While it is true that Plaintiffs will be prejudiced by the decision to dismiss this case with prejudice, the harm to Plaintiffs is more than outweighed by the harm to Chrysler and to the legal system as a whole that would flow from any decision to allow Plaintiffs to continue to prosecute their case under these circumstances.

Appendix B

Conclusion

The Magistrate Judge correctly concluded that Mr. Gorman made false statements in the affidavit he filed on April 9, 2003 and that those statements led, in part, to the Court order that required Chrylser to extend additional floor plan financing to Plaintiffs, which in turn caused Chrysler to suffer additional losses. The Magistrate Judge correctly concluded that Mr. Gorman misled Chrysler during discovery which resulted in the computers that contained valuable evidence not being preserved for this dispute. The Magistrate Judge correctly concluded that Mr. Gorman either lied or misled Defendant regarding the notes which formed the basis for the allegations of discriminatory intent in the Complaint to the extent Defendant is able to pursue them.

Because Defendant can not properly defend against allegations that have been supported by such lies, and cannot build its counterclaims against Plaintiffs without evidence that has been destroyed or concealed, monetary sanctions can not suffice to repair the harm inflicted on this case and on the judicial system as a whole. The harsh sanction of dismissal of this case is warranted and that will be the order of this Court. The Court denies the Motion for Default Judgment on the Counterclaims and those counterclaims will remain in the case.

Appendix B

The Court adopts the Report and Recommendation and its reasoning in its entirety. The Complaint is dismissed with prejudice.

So ordered.

s/ Virginia M. Kendall
Virginia M. Kendall,
United States District Judge
Northern District of Illinois

Date: September 6, 2006

APPENDIX C — REPORT AND RECOMMENDATION OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION FILED JUNE 14, 2005

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS EASTERN DIVISION

Case No.: 03 C 760

Judge Wayne R. Andersen

Magistrate Judge
Arlander Keys

RIDGE CHRYSLER JEEP L.L.C., d/b/a MARQUETTE CHRYSLER JEEP and SALES, INC., d/b/a DODGE OF MIDLOTHIAN,

Plaintiffs,

vs.

DAIMLER CHRYSLER SERVICES NORTH AMERICA, L.L.C. d/b/a CHRYSLER FINANCIAL COMPANY, L.L.C.,

Defendant.

TO: THE HONORABLE WAYNE R. ANDERSEN, UNITED STATES DISTRICT JUDGE

Appendix C

REPORT AND RECOMMENDATION

This case is before the Court on two motions for sanctions filed by the defendant, Daimler Chrysler Services North America, L.L.C. d/b/a Chrysler Financial Company, L.L.C. ("Chrysler").

The first motion is a Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for Making False Statements, and the second is a Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for Failure to Produce and Preserve Evidence.

In its first motion, Chrysler claims that Gerald Gorman, the owner of the dealership plaintiffs, made certain false statements during the course of the proceedings in this case. As a sanction for those statements, Chrysler seeks dismissal of the Complaint; alternatively, Chrysler asks the Court to order Mr. Gorman to reimburse Chrysler for the losses (including attorney's fees and costs) it incurred as a result of those statements. In its second motion, Chrysler claims that the plaintiffs failed to produce and preserve certain key pieces of evidence, and, as a sanction for that failure, Chrysler seeks dismissal of the Complaint; alternatively, Chrysler seeks an instruction to the jury that it may infer that any evidence the plaintiffs lost or destroyed would have been favorable to Chrysler and damaging to the plaintiffs.

Appendix C

Factual Background & Procedural History

Gerald Gorman owned and operated an automobile dealership called Ridge Chrysler Jeep L.L.C., formerly doing business as Marquette Chrysler Jeep at 65th Street and Western Avenue in Chicago, Illinois; he also owned and operated Sales, Inc., doing business as Dodge of Midlothian, in Midlothian, Illinois (collectively referred to as "the dealerships"). Both dealerships had dealer franchise agreements with DaimlerChrysler Motors Company.

In June of 2002, Chrysler and Midlothian executed a "Master Loan and Security Agreement," pursuant to which Chrysler agreed to provide financing to allow Midlothian's customers to buy new and used cars, in exchange for being given a security interest in those cars. According to Midlothian, despite the Agreement, Chrysler advised that it would not provide financing for non-suburban African-American customers, regardless of their creditworthiness. Moreover, the dealerships claimed, when they refused to go along with Chrysler's attempts to discriminate and racially profile customers, Chrysler penalized the dealerships in ways that wreaked financial havoc on the dealerships, forcing Marquette out of business entirely, and harming Midlothian substantially. Specifically, the plaintiffs allege that Chrysler terminated Midlothian's lines of credit and restricted its ability to order and acquire cars, all in retaliation for Midlothian's refusal to go along with Chrysler's discriminatory practices.

Appendix C

Chrysler acknowledged that, on March 21, 2003, it terminated Midlothian's lines of credit and demanded the surrender of Chrysler's vehicle collateral. But it claimed that it did so because, after conducting a limited financial review of the dealership, it realized that the plaintiffs had misrepresented Midlothian's financial condition, including overstating the dealership's working capital, failed to provide financial statements, and siphoned off more than a million dollars from Midlothian to pay debts owed to Mr. Gorman.

1. *The Lawsuit*

On February 3, 2003, the dealerships sued Chrysler, alleging that Chrysler adopted an internal corporate policy of refusing to provide financing to non-suburban African-American car buyers, regardless of their creditworthiness, and then punished the dealerships for refusing to go along with that discriminatory practice. The dealerships' complaint piggybacked on another case filed that same day by a putative class of minority plaintiffs who allege that Chrysler engaged in predatory lending practices by refusing to give lower financing rates to otherwise qualified minority car buyers. Chrysler has denied any wrongdoing; Chrysler also filed a Verified Counterclaim against both dealerships, and Gerald Gorman and his wife, Elizabeth Gorman, alleging breach of the Master Loan and Security Agreement, as well as other contracts executed by the parties.

Appendix C

2. *The TRO Request and the Stipulated Order*

On April 4, 2003, the dealerships moved for a TRO and for a preliminary injunction, asking the Court to require Chrysler to reinstate Midlothian's lines of credit and to remove certain restrictions it had implemented on the dealership's ability to order and buy cars. Chrysler opposed the plaintiffs' motion, arguing, *inter alia*, that the plaintiffs had offered no valid reason for forcing Chrysler to continue lending them money, especially when Midlothian should have had other options for financing its floor plan.[1] Specifically, Chrysler argued as follows:

> As for the elements necessary to show an entitlement to either a TRO or preliminary injunction, Midlothian has plainly failed to meet its burden of proof. . . . Midlothian has not shown any irreparable harm at all. Chrysler Financial is not the only floor plan lender for DaimlerChrysler products. Indeed, Marquette floor planned its cars with a local Chicago bank. Midlothian, evidently by choice, has apparently not even tried to get floor plan financing from another lender, raising the question "Why?" If other lenders won't advance Midlothian the money to take out the Chrysler Financial debt, there must be a reason — yet another fact that Midlothian fails to tell the Court.

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1. "Floor plan" financing refers to the financing of the dealership's acquisition and inventory of new and used cars.

Appendix C

Chrysler's Memorandum in Opposition to Motion for Temporary Restraining Order and Preliminary Injunction, p. 2.

Judge Anderson, the district judge to whom the case is assigned, held a hearing on the motion on April 8, 2003. After hearing from both sides, Judge Andersen preliminarily noted:

> I think a good interim solution, while we determine whether or not these facts are true and whether or not there is any connection — and I have my doubts — is to permit — is to grant a TRO to the plaintiffs, requiring that Chrysler live up to the obligations that it undertook in its agreements with Midlothian. However, with several important qualifications. First, I think, for example, Mr. Gorman has offered to put the million dollars back in to bring the working capital back up. Fine, let him put the million dollars back in. . . .
>
> And that the parties immediately undertake an updated audit to find out exactly what the financial status of Midlothian is and potentially, I suppose, even Mr. Gorman, although I don't know to what extent his personal finances are important here.
>
> And — and any other operational checks or oversight that might be required to assure

> Chrysler Financial that while it was financing the purchase of new vehicles, that its position was not going to erode. I think that would be — that is essential, not just for the company, but the company has shareholders and so on who are entitled to make sure that its assets are not just shoved out the door.

Transcript of April 8, 2003 Hearing, pp. 17-18 (attached as Exhibit C to Chrysler's Motion for Sanctions for False Statements). Presumably in part to allay the concerns raised by Judge Andersen, on April 9, 2003, the plaintiffs filed a reply brief, and submitted along with it an affidavit from Mr. Gorman. The affidavit states, in part, as follows:

> Following the results of a "limited financial review" of Midlothian, conducted by DaimlerChrysler Services North American (Chrysler Financial) in December [2002], approximately $925,000.00 was invested into the Midlothian dealership as additional working capital. This was an investment of personal money and this capital investment is wholly unencumbered. The source of the capital investment was not a loan from a third party that would require repayment from dealership assets, nor was it a withdrawal from a bank account. The sources of the capital investment were monies obtained from the sale of stock certificates and a direct investment from a long time business associate.

Affidavit of Gerald Gorman, ¶2. He further stated that "[a]fter Midlothian was placed on financial hold by defendant, I went to two different banks to try to take out a loan and to refinance the floor plan at Midlothian. I was turned down by both banks due to issues related to the financial hold and the pending litigation with defendant." *Id.* ¶12.

Based at least in part on these representations, Judge Anderson determined that it would be appropriate for Chrysler to extend additional floor plan financing to Midlothian, and the Court directed the parties to attempt to agree to the specifics of a deal. On April 11, 2003, Judge Anderson entered an Order requiring Chrysler to provide wholesale floor plan financing to Midlothian for a period of not more than 180 days. *See* Order entered April 11, 2003, ¶1 (Attached as Exhibit 0 to Chrysler's Motion for Sanctions). The Order also allowed Chrysler to keep representatives on-site at the dealership and to otherwise monitor the dealership's business operations. *Id.*, ¶¶4-7, 10. The Order also noted that "Midlothian represents and warrants that a $925,000 equity capital infusion has been made, which is unencumbered and not . . . subject to repayment by Midlothian to the investment source." *Id.*, ¶9.

Chrysler subsequently sought the opportunity to conduct a limited financial review of Midlothian's operations, and, on September 9, 2003, Judge Anderson granted Chrysler's request. Additionally, the Court approved a plan for the parties to conduct discovery on the remainder of the case.

3. *Discovery*[2]

The discovery phase of this litigation, which was handled by this Court, on referral from Judge Anderson, proceeded apace, with a fair — though not extraordinary — degree of Court intervention. Two days after filing the lawsuit, counsel for the plaintiffs, Steven Berman, wrote to Chrysler advising the company that the lawsuits had been filed and instructing it

> not to destroy, conceal or alter any paper or electronic files and other data generated by/or stored on computers and storage media (e.g., hard disks, floppy disks, backup tapes), or any other electronic data, such as voice mail that may relate to these lawsuits. Failure to comply with this notice can result in severe sanctions being imposed by the Court for spoliation of evidence or potential evidence.

February 5, 2003 Letter from Steven W. Berman of Hagens & Berman to DJ Culkar, Staff Counsel at DaimlerChrysler Services North America (attached as Exhibit 8 to Chrysler's Reply Brief in Support of its Motions for Sanctions for Failure to Produce and Preserve Evidence). The letter spans seven pages and explains, in great detail, the steps that should be taken

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2. The Court has no intention of revisiting everything that transpired during the discovery phase of this litigation; rather, the Court will highlight those aspects of the discovery process that are relevant and necessary to give context to the motions now before the Court.

— or not taken — to prevent spoliation and to avoid the possibility of sanctions. On March 3, 2003, Mr. Berman sent another letter, this time to Chrysler's counsel at Mayer Brown Rowe & Maw and Thompson Coburn LLP, advising of the first letter and seeking a response delineating what steps Chrysler had taken to preserve evidence. *See* March 3, 2003 Letter from Steven W. Berman to Lucia Nale and William R. Bay (attached as Exhibit 9 to Chrysler's Reply Brief). Two days later, Mr. Berman sent Mr. Bay another letter stating that "[w]e will preserve all evidence as required by the Rules of Civil Procedure and we assume Chrysler is doing the same per our earlier agreement." March 5, 2003 Letter from Steven W. Berman to William R. Bay (attached as Exhibit 10 to Chrysler's Reply Brief).

Shortly thereafter, the parties exchanged discovery requests. Among other things, Chrysler asked the plaintiffs to produce "all monthly, quarterly, and annual financial statements for Midlothian, including, but not limited to, balance sheets, income statements, profit and loss statements, statements of cash flows, etc., since September 2000, both in paper and electronic form." The plaintiffs objected, arguing that the documents requested were in Chrysler's custody and control, but they nonetheless agreed to produce "relevant, non-privileged responsive documents currently in its possession." *See* Plaintiff's Objections and Responses to Defendant's First Request for Production Directed to Plaintiff Sales, Inc., ¶24 (attached as Exhibit 1 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence).

Appendix C

The production from the plaintiffs was, at least in Chrysler's view, insufficient, and counsel for Chrysler worked more informally to obtain additional responses from the plaintiffs. In an email dated February 18, 2004, counsel for Chrysler asked plaintiffs' counsel to

> please let us know whether Marquette and Midlothian have any electronic records, computer data files, or e-mails responsive to our requests for production. To date, no such electronic records, computer files, or e-mails have been produced by your clients (except apparently for the 1999 Marquette Reynolds & Reynolds tapes).[3] I suspect that your clients' financial information — including their general ledgers — was stored on your clients' computers.

See February 18, 2004 email from Jeffrey R. Fink to Chris O'Hara (attached as Exhibit 3 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). Mr. O'Hara immediately responded

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3. According to Gerald Gorman, Reynolds & Reynolds is a company that provides computer hardware, software and forms for automobile dealerships; both dealerships involved in this case used the company's services. It was Mr. Gorman's understanding that the company provided the software, the dealerships entered their information into it, and Reynolds & Reynolds provided forms, etc. to track and keep the information. *See* Gorman Deposition, p. 486. *See also* Transcript of Deposition of Kathleen Manheim, p. 51 (the dealerships leased their computer from Reynolds & Reynolds, which also provided the software).

with a short "Will do." *See* February 18, 2004 email from Chris O'Hara to Jeffrey R. Fink (also included in Exhibit 3).

Chrysler's attorneys also sought discovery through Reynolds and Reynolds, which notified them by letter dated March 4, 2004 that, although Reynolds and Reynolds had leased hardware (including a server) and software to the Marquette and Midlothian dealerships, Reynolds and Reynolds "does not maintain information or data generated by these dealers' use of the Reynolds hardware and software. This data, including all of the information identified in Exhibit A to your subpoena, is the property of the dealers. Reynolds does not keep or maintain such information." *See* March 4, 2004 Letter from Timothy G. Nickels to Eileen Letts and Julia Barnhardt (attached as Exhibit B to Plaintiffs' Response to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence).

Despite Reynolds and Reynolds' representation that the information Chrysler sought should be in the plaintiffs' possession, Chrysler still received nothing from the plaintiffs on this issue. And, by mid-March 2004, Chrysler's attorneys were considerably less cordial. On March 17, Mr. Fink wrote to Mr. O'Hara to urge the plaintiffs to respond to Chrysler's outstanding discovery responses and to highlight the particular areas of concern; he wrote:

> As discussed in one of my February 16, 2004 letters, Plaintiffs need to produce all

> Reynolds & Reynolds materials. In response to our subpoena, Reynolds & Reynolds has indicated that it doesn't have any data tapes/ cartridges for Midlothian or Marquette and that all such materials were provided to Midlothian and Marquette. Plaintiffs should have no difficulty locating these materials.
>
> Additionally, Marquette has failed to produce its monthly journals and schedules for 2000 and 2001. This is highly suspect given that Marquette produced its monthly journals and schedules for 1999 and 2002. Please produce the 2000 and 2001 monthly journals and schedules for Marquette promptly.

See March 17, 2004 email from Jeffrey R. Fink to Chris O'Hara (attached as Exhibit 4 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). Mr. O'Hara responded as follows:

> It is my understanding from my client that all Reynolds & Reynolds material in the possession of the dealerships or owner have been produced. I will double check this with my client. To the extent that there are remaining items contained in Reynolds & Reynolds computers or databases, my client no longer has access to such computers or databases, as they were shut off and denied access to the Reynolds & Reynolds system long ago.

> As for the Marquette journals and schedules, it is also my understanding that we gave you everything remaining from Marquette, so if there were journals and schedules from 2000 and 2001 from Marquette in its possession, they would have been produced. In fact, Gorman says he remembers finding the Marquette journals and schedules while going thru one of the Midlothian offices with Frank Buckley — and pointing that out to Frank — when the materials were first produced for copying.[4] I'm going to double check with my client on this as well.

See March 17, 2004 email from Chris O'Hara to Jeffrey R. Fink (also included in Exhibit 4). In another email dated April 2, 2004, Mr. O'Hara wrote:

> [a]s I've previously told you, it is my understanding from my clients that all Reynolds & Reynolds material in the possession of the dealerships or owner have been produced. To the extent that there are remaining items contained in Reynolds & Reynolds computers or databases, my client no longer has access to such computers or databases, as they were shut off and denied access to the Reynolds & Reynolds system

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4. At his deposition, Mr. Gorman flip-flopped on the issue, testifying that he had no recollection of specifically seeing the 2000 and 2001 records. *See* Gorman Deposition, p. 509-511.

> long ago. If Reynolds & Reynolds is able to access this information, we would, of course, be willing to cooperate in any way we can to allow you access to any information regarding the 2 dealerships still available through the system. We simply no longer have access to it.
>
> * * *
>
> As for financial records on hard drives or discs, my clients again have none. The only accounting software used by the dealerships was through Reynolds & Reynolds, and, again, my clients no longer have access to this system. Again, if there are financial records available through the Reynolds & Reynolds system, we would have no problem in allowing Chrysler access to those records if Reynolds & Reynolds can access it.

Email from Chris O'Hara to Jeffrey R. Fink dated April 2, 2004 (attached as Exhibit 5 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence).

On April 7, 2004, Mr. Fink wrote to Mr. O'Hara, noting that, despite repeated requests, the plaintiffs had not produced Marquette's 2000 and 2001 journals and schedules. *See* April 7, 2004 Letter from Jeffrey R. Fink to Christopher A. O'Hara (attached as Exhibit 6 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). Mr. O'Hara responded with

an email "confirm[ing] that the dealerships apparently are missing the journals and ledgers from Marquette that you have been asking about from 2000 and 2001." *See* May 14, 2000 email from Chris O'Hara to Jeffrey R. Fink and William Bay (attached as Exhibit 7 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). Mr. O'Hara also addressed the issue of the computer databases; he wrote:

> I do have messages via voice mail and email into Tim Nickels, counsel for Reynolds and Reynolds to see about getting access to the Reynolds and Reynolds system to retrieve the data you've requested. . . . As I've indicated previously on several occasions, we have turned over all the hard copy Reynolds and Reynolds materials the dealerships have and the problem with retrieving the rest is the fact that the dealerships have not had access to the Reynolds and Reynolds system since they went out of business. I will let you know as soon as I hear back from Mr. Nickels.

See May 14, 2004 email from Chris O'Hara to Jeffrey R. Fink (attached as Exhibit 7 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). Chrysler never did get the dealerships' computer; nor did Chrysler ever get the 2000 and 2001 journals and schedules for Marquette.

Discovery closed in December 2004. Shortly thereafter, on January 26, 2005, Chrysler filed its Motion

for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for False Statements, and its Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for Failure to Produce and Preserve Evidence. Judge Anderson referred both motions to this Court on February 9, 2005, and they were fully briefed as of April 1, 2005.

DISCUSSION

The Court is unquestionably vested with the inherent power to sanction litigants for bad-faith and fraudulent conduct. *See, e.g., REP MCR Realty v. Lynch*, 363 F.Supp.2d 984, 998 (N.D. Ill. 2005) (citing *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43 (1991)). This includes "the power, in appropriate cases, to impose the sanction of dismissal with prejudice." *Id.* (citing *Diettrich v. Northwest Airlines, Inc.*, 168 F.3d 961, 964 (7th Cir. 1999)). Dismissal is a harsh sanction, however, and should, therefore, be imposed rarely, and only after the Court has considered whether a less severe sanction might be adequate and appropriate. *See Lynch*, 363 F.Supp.2d at 999. "In deciding what measure of sanctions to impose, the district court should consider 'the egregiousness of the conduct in question *in relation to all aspects of the judicial process.*'" *Dotson v. Bravo*, 321 F.3d 663, 667 (7th Cir. 2003) (quoting *Barnhill v. United States*, 11 F.3d 1360, 1368 (7th Cir. 1993)) (emphasis in original). To justify a dismissal based upon a litigant's bad behavior, or upon the failure of prior sanctions to cure that bad behavior, the record of such behavior must be clear. *Maynard v. Nygren*, 332 F.3d 462, 468-69 (7th Cir. 2003).

Appendix C

A. *The Motion for Sanctions for False Statements*

At the outset, the Court notes that, if, as Chrysler claims, Mr. Gorman lied in the affidavit he filed with the Court, the case should be dismissed. *See ABF Freight System, Inc. v. National Labor Relations Board*, 510 U.S. 317, 323 (1994) ("False testimony in a formal proceeding is intolerable. We must neither reward nor condone such a 'flagrant affront' to the truth-seeking function of adversary proceedings.") (citing *United States v. Mandujano*, 425 U.S. 564, 576-77 (1976)). In connection with its first motion, Chrysler claims that Mr. Gorman made three separate and distinct misrepresentations, the first dealing with a supposedly-unencumbered $925,000 capital investment, the second dealing with Mr. Gorman's supposed attempts to obtain replacement floor plan financing, and the third dealing with a subordination agreement supposedly signed by Mr. Gorman.

1. *The $925,000 "Capital Investment"*

Chrysler first challenges the statement Mr. Gorman made in his April 9, 2003 affidavit that he personally had recently made a $925,000 capital investment into the dealerships, and that his investment was unencumbered. In fact, according to Chrysler, the "investment" turned out to be a $750,000 loan from Edward Vrdolyak, and a $175,000 payment from Patrick Fitzgibbon to the dealership, to cover the sale of some First Suburban Bancorp stock. According to Chrysler, the loan from Mr. Vrdolyak had to be repaid, and was,

thus, encumbered, and the money from Mr. Fitzgibbon was not an influx of capital, but the liquidation of an asset already held by the dealership.

Turning first to the "investment" from Mr. Vrdolyak, the plaintiffs argue that the testimony of both Mr. Gorman and Mr. Vrdolyak supports the plaintiffs' story that the money was unencumbered. The evidence, however, says otherwise. At his deposition, Mr. Vrdolyak admitted that, on December 27, 2002, he wrote a check for $750,000 to Midlothian Dodge. Transcript of Deposition of Edward Vrdolyak, p. 96 (attached as Exhibit V to Chrysler's Motion for Sanctions). He further testified that he borrowed that money from First Suburban Bank to loan to Midlothian, and that, at least as of the time of his deposition, on September 29, 2004, he personally was making payments on that loan. *Id.* at 97, 99-100. Mr. Vrdolyak further testified that he and Mr. Gorman signed a written agreement about the $750,000; that agreement provided that, in exchange for the $750,000 loan from Mr. Vrdolyak to Midlothian Dodge, Midlothian Dodge would give Mr. Vrdolyak "as collateral used cars subject to all UCC filings as directed and controlled by First Suburban National Bank and its president. . . ." *Id.* at 100-104. The agreement further provided that Mr. Vrdolyak "will immediately receive ownership documents concerning the aforestated business and companies, as well as pro rata percentages of profits and losses." *Id.* at 104.

Mr. Vrdolyak testified that, technically, he loaned the money to the dealership, but that, in his view,

Mr. Gorman was also personally responsible to repay the loan; he testified that Mr. Gorman had given him his personal guarantee that if the dealership could not repay the loan, Mr. Gorman would. *Id.* at 107. Later in his deposition, Mr. Vrdolyak testified that, despite this guarantee, he did not think that his loan in any way encumbered Midlothian Dodge's assets; he testified that he had orally waived the collateral and told Mr. Gorman not to "worry about it." *Id.* at 108-112, 115. He testified that the money was not a gift, it was an interest-free loan that was to be repaid by Mr. Gorman "[w]hen he got some money." *Id.* at 124-125. He testified that, as of the date of his deposition, he was still owed $750,000 by Midlothian Dodge and/or by Gerald Gorman. *Id.* at 126. On further questioning, Mr. Vrdolyak testified that it appeared that he was paid some interest on the $750,000 loan. *Id.* at 129-136.

At his deposition, Mr. Gorman similarly testified that, on December 27, 2002, Mr. Vrdolyak wrote a $750,000 check to Midlothian Dodge, and that the money was deposited into the company's account at First Suburban Bank. Transcript of Deposition of Gerald Gorman, pp. 2166-69 (attached as Exhibit G to Chrysler's Motion). He testified, however, that, in his view, the money was really meant for him personally; he testified that "[s]o even though the check was written out to Midlothian Dodge, it clearly was meant to be assistance to me personally with no UCC filings I told him and none were ever executed." Gorman Dep. p. 2171. He testified that he "disagree[d] with Mr. Vrdolyak's testimony in the sense that I look at it as

the loan — that the money was — it's a legal issue, but the money was for me. He was helping me out as a friend." Gorman Dep., p. 2171. Mr. Gorman admitted that he "might have given [Mr. Vrdolyak] some money for his return on his investment." Gorman Dep., pp. 2206-07. He admitted that Midlothian's cash disbursements journal showed payments being made to Mr. Vrdolyak throughout 2003, and he admitted that those payments "most likely were" payments on the $750,000 loan made by Mr. Vrdolyak. Gorman Dep., pp. 2207-12.

Based upon this evidence, the Court agrees with Chrysler that the $750,000 provided by Mr. Vrdolyak was a loan that needed to be repaid; it was not, as Mr. Gorman stated in his affidavit, "a direct investment from a long time business associate."

Initially, the Court notes that the plaintiffs took great pains to avoid having to reveal that Mr. Vrdolyak was behind the money. At the hearing on the TRO motion, Chrysler's attorney specifically requested that, to ensure Chrysler's position, in addition to the injection of a million dollars, Chrysler would want "to make sure that it is unencumbered. We want to know what the source of funds is. And we want to make sure that if there is any kind of loan back, if it is — if it is going to be repaid, that it is subordinated." Transcript of Proceedings of April 8, 2003, p. 24. Counsel for the plaintiffs resisted, saying that they would "sign an affidavit that the money is unencumbered," but that "the source of funds, under the circumstances, that is

irrelevant and immaterial." *Id.* And, in his affidavit, Mr. Gorman simply said that the money was "a direct investment from a long time business associate." Affidavit of Gerald Gorman, ¶2. It was not until the issue was forced through discovery that the plaintiffs revealed the identity of the "business associate" — and even then, they initially resisted such disclosure; in response to Chrysler's request to produce documents regarding the investment, the plaintiffs objected "on the basis that the request calls for the production of documents that are in Defendant's custody and control, or that are protected by work product or attorney-client privilege," — none of which would have been true. They also objected on the grounds that the request "seeks documents that are neither relevant nor reasonably calculated to lead to the discovery of admissible evidence." *See* Plaintiff's Objections and Responses to Defendant's First Request for Production Directed to Plaintiff Sales, Inc., ¶50 (attached as Exhibit 1 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence).

Mr. Vrdolyak and Mr. Gorman also took great pains to dance around the true nature of the transaction, sometimes stumbling after saying the word "loan" as if they had been warned to avoid even speaking the word at all costs. Both witnesses tried to characterize the transaction as "one friend simply helping out another friend." But, significantly, neither Mr. Vrdolyak nor Mr. Gorman ever even remotely hinted that the loan would be forgiven; both clearly anticipated that Mr. Vrdolyak would get his money back. Indeed, to make the loan in

the first place, Mr. Vrdolyak had himself taken out a $750,000 loan from First Suburban Bancorp, and then handed the proceeds of that loan over to Midlothian Dodge and Gerald Gorman. And Mr. Vrdolyak testified that he was making payments on that loan to First Suburban, though the evidence actually suggests that Midlothian Dodge may have been making those payments, whether directly or indirectly.

In short, although the relationship between Mr. Vrdolyak and Mr. Gorman may have allowed the $750,000 loan to be repaid at a lower interest rate than would have been permitted by a bank and on a more flexible schedule than would have been permitted by a bank, there is no question that, at the end of the day, the money had to be repaid to Mr. Vrdolyak.

Moreover, it is equally clear that, to the extent payments were being made on that loan, they were being made out of the coffers of the dealership, not out of Mr. Gorman's personal coffers. And, indeed, the only document that exists to evidence the transaction expressly states that the dealership is on the hook to repay the loan. To the extent Mr. Vrdolyak and Mr. Gorman orally altered the terms of the transaction after-the-fact, there is nothing in the way of documents to reflect that. Thus, contrary to Mr. Gorman's statement in his affidavit, the money was very much encumbered, at least on paper and at least in the eyes of the law, whether or not Mr. Vrdolyak would ever have attempted to foreclose on the obligation.

Appendix C

In addition to the $750,000 from Mr. Vrdolyak, Mr. Gorman's affidavit states that the "capital investment" also consisted of "monies obtained from the sale of stock certificates." *See* Gorman Affidavit, ¶2. By all accounts, this reference is to a transaction in which Mr. Gorman sold to Patrick Fitzgibbon certain shares of First Suburban Bancorp stock. At his deposition, Mr. Gorman testified that, in 2000 or 2001, he personally purchased about $150,000 worth of stock in First Suburban Bancorp; he testified that it was a personal purchase, not a corporate purchase. Transcript of Deposition of Gerald Gorman taken October 8, 2004, pp. 2078-2080 (attached as Exhibit 1 to Plaintiffs' Response to Chrysler's Motion for Sanctions for False Statements). Mr. Gorman testified that he sold the stock to Mr. Fitzgibbon on December 20, 2002; he testified that the stock certificates were held by him and his wife, and that he assigned them to Mr. Fitzgibbon on December 20, 2002. Gorman Dep., pp. 2080-2081, 2550-2552. But Mr. Gorman also admitted that, in its October 2003 financial statement, the Midlothian dealership was claiming that it owned $150,000 in First Suburban stock — the same stock that he and his wife had supposedly transferred to Mr. Fitzgibbon nine months earlier; he testified that the dealership claimed ownership of the stock in each of the monthly financial statements that it submitted to Chrysler in 2003. Gorman Dep., pp. 2554-2556.

Mr. Fitzgibbon testified that he bought stock in First Suburban Bancorp from Mr. Gorman; he testified that, on or about December 20, 2002, Mr. Gorman signed the

stock certificates over to him. Transcript of Deposition of Patrick J. Fitzgibbon taken December 9, 2002, pp. 301-302, 305-307. Mr. Fitzgibbon testified that, in exchange for the stock certificates, he gave Mr. Gorman a cashier's check for $175,000. *Id.*, p. 308-309. He further testified that he did not consider this to be a loan, but an outright purchase; he also testified that there was no agreement or understanding that at some future point Mr. Gorman would buy the stock back from him. *Id.*, p. 309.

Joseph Hogan, the president of First Suburban Bancorp, testified that Mr. Gorman and his wife bought stock in the bank, and that it was purchased and held by them personally, not by the dealership. Transcript of Deposition of Joseph D. Hogan taken November 19, 2004, p. 138 (attached as Exhibit H to Chrysler's Motion for Sanctions for False Statements). Mr. Hogan testified that the Gormans purchased $50,000 worth of First Suburban stock in one transaction, and another $100,004 worth of First Suburban stock in another transaction. Hogan Dep., pp. 138-140. The subscription agreements similarly reflect that the First Suburban Bancorp stock was purchased by Gerald and Elizabeth Gorman as joint tenants. *See* Subscription Agreement dated December 16, 2000 (attached as Exhibit 110 to Chrysler's sanctions motion); Memorandum of Agreement dated November 29, 2001 (attached as Exhibit 113 to Chrysler's sanctions motion). Mr. Hogan also testified that, as of the date of his deposition — November 19, 2004 — Mr. and Mrs. Gorman remained the holders of record of this stock. Hogan Dep. at 143-44.

Appendix C

The evidence unquestionably suggests that the stock transaction was handled in a sloppy fashion — Ms. Gorman never signed the certificates to transfer ownership of the stock, the bank was never advised that there was a new holder of record, and Mr. Gorman continued to allow the stock to remain on his and his dealership's financial statements even after the stock was sold. But it is not clear that Mr. Gorman handled the transaction this way because he was trying to pull a fast one or trying to hide something or misrepresent something to Chrysler.

Mr. Gorman is quick to point out that Chrysler has always refused to recognize the stock as an asset of the dealership because it was held in his name, and that it is now trying to have it both ways — on the one hand Chrysler refused to consider the stock as an asset of the dealership because it was held in his name, and on the other hand Chrysler now says the stock belonged to the dealership such that selling the asset did nothing to increase the dealership's net worth. But one could just as easily argue that Mr. Gorman is trying to have it both ways — claiming on the one hand that he sold the stock and put the proceeds from that sale into his dealership, but claiming on the other hand that the stock remained a personal asset and an asset of the dealership long after the sale was supposedly accomplished.

Although the question is murky, the record does not clearly show that Mr. Gorman lied about the nature of the $175,000 he received from Mr. Fitzgibbon; if he is telling the truth about the stock purchase — a

possibility that is supported by some evidence in the record, the $175,000 would have been unencumbered, as he stated in his affidavit. The same is not true of the statement about the nature of the $750,000 from Mr. Vrdolyak; the record clearly shows that it *was* encumbered, and his statement to the contrary was false.

2. *Replacement Floor Plan Financing*

Chrysler next challenges the statement Mr. Gorman made in his April 9, 2003 affidavit that, "[a]fter Midlothian was placed on financial hold by defendant, I went to two different banks to try to take out a loan and to refinance the floor plan at Midlothian." *See* Affidavit of Gerald Gorman, ¶12 (attached as Exhibit A to Chrysler's Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for False Statements). He further states that, both times, he was "turned down . . . due to issues related to the financial hold and the pending litigation with defendant." *Id.* This statement, or the gist of it, appears to have played a significant role in Judge Anderson's decision to enter the Order requiring Chrysler to continue to extend floor plan financing to Midlothian while the parties continued to work toward resolution of their issues. And Chrysler claims that it was all a lie.

The plaintiffs argue that, when properly construed, the evidence shows that Mr. Gorman approached First Suburban Bank about replacement floor plan financing. And Mr. Gorman has also now submitted another

affidavit, dated March 14, 2005, stating that, "[i]n addition to First Suburban Bank, I also contacted Pullman Bank about replacement floor plan financing. I met with a representative of Pullman Bank after Midlothian was placed on financial hold by the defendant, but before I executed the affidavit of April 9, 2003." Affidavit of Gerald Gorman dated March 14, 2005 (attached as Exhibit 6 to Plaintiffs' Opposition to Chrysler's Motion for Sanctions for False Statements).

In assessing the veracity of Mr. Gorman's statement about his alleged attempts to obtain replacement floor plan financing, the Court must look at the time period from December 2002, when Chrysler placed Midlothian on financial hold, and April 9, 2003, when Mr. Gorman executed his affidavit. The question is whether Mr. Gorman did, as he stated in his affidavit, approach banks about floor plan financing during this time.

At his deposition on October 7, 2004, Mr. Gorman was asked whether, during the last months of 2002, he had attempted to borrow money for Midlothian from anyone other than Chrysler and Mr. Vrdolyak, from whom he had obtained the $750,000 loan:

Q: The question is: Did you try to borrow money from First Suburban to put into the dealership?

A: No, sir.

Q: Did you try to borrow it from anyone else?

A: I asked Chrysler.

Q: Did you go to anybody else to borrow money in this time frame in the fall of 2002 to put into the dealership?

A: No, sir.

Q: So the only person you went to is Mr. Vrdolyak?

A: Uh—huh.

* * *

Q: I want to know who else you went to borrow money from besides either Chrysler or Mr. Vrdolyak in the fall of 2002.

A: At this time in 2002, no.

Q: I am talking about in the fall of 2002, September, October, November, December.

A: No.

Q: Nobody else?

A: No.

Gorman Dep., pp. 2172-74. Later on in the deposition, Mr. Gorman testified that he had contacted First Suburban Bank about floor plan financing, but that he did not do so until after "the 180-day Order" was entered, *id.*, pp. 2585-86; that Order was entered on April 11, 2003, two days *after* he signed his affidavit.

As part of the discovery process that occurred after Judge Anderson entered the April 11, 2003 Order, Chrysler posed an interrogatory to the plaintiffs asking them to "[d]escribe in detail each and every attempt by Midlothian to obtain floor plan financing from someone other than Chrysler Financial, including, but not limited to, the two alleged attempts that are mentioned in paragraph 12 of the Affidavit of Gerald Gorman executed on April 9, 2003." *See* Plaintiff's Responses to Defendant's Third Set of Interrogatories Directed To Plaintiff Sales, Inc. (attached as Exhibit 615 to Chrysler's Motion for Sanctions for False Statements). In a maneuver that probably seemed clever to the plaintiffs at the time, the plaintiffs answered the interrogatory by skirting the question somewhat; they responded:

> [i]n the weeks following the Agreed Order dated April 15, 2003, Shawn Temple contacted numerous banks by telephone in an attempt to obtain financing in lieu of Chrysler Financial, including but not limited to Fifth Third Bank (contact: Kevin Point), Comerica's Oak Brook office (contact: Mike, whose last name is unknown), World Omni (contact: Russell Wolf), Bank One and Pullman Bank.

> During each of these conversations, Mr. Temple was asked the identity of the lender that was currently financing the floor plan. He explained that it was Chrysler Financial. Each time, the lender would inquire why he was looking for a new lender. Mr. Temple was thus forced to disclose the lawsuit. At that point, each lender either told Mr. Temple that they were not interested or that they would get back to him (and later orally declined interest in providing financing).

Id. At his deposition, Mr. Gorman confirmed that this interrogatory answer is true and correct. Gorman Deposition, p. 2585. Mr. Gorman also testified that he had talked to someone at Fifth Third Bank, but he could not recall when he did so. His testimony suggests, however, that he talked to Fifth Third before Chrysler placed Midlothian on financial hold, in December 2002, which would be consistent with the earlier portions of his deposition testimony quoted above. Gorman Dep., pp. 2581-2583.

Mr. Gorman's statement about replacement floor plan financing is, without a doubt, the most blatant of the lies alleged. There is no evidence in the record to support the statement Mr. Gorman made in his affidavit that, after Chrysler placed Midlothian on financial hold, he attempted to obtain replacement floor plan financing at other banks, and was turned down. His own deposition testimony contradicts this statement, as does all of the documentary evidence in the record. This evidence

makes clear that any attempts to obtain replacement floor plan financing came after the affidavit was written. Based upon this, the Court can only conclude that Chrysler is right: Mr. Gorman lied in his affidavit.[5] What's worse, his lies served, at least in part, to persuade the Court that the April 11, 2003 Order should issue, thereby subjecting Chrysler to the risk that it could — and would — lose more money on Midlothian and Mr. Gorman.

Deliberately providing false information to the Court to achieve one's objective cannot be condoned and certainly warrants the harshest of sanctions. As the Seventh Circuit noted in *Dotson v. Bravo*, 321 F.3d 663, 667 (7th Cir. 2003), "'[t]here are species of misconduct that place too high a burden . . . for a court to allow a case to continue.'" (quoting *Barnhill v. United States*, 11 F.3d 1360, 1368 (7th Cir. 1993)). And the utter lack of respect for judicial proceedings that is reflected by Mr. Gorman's lies is no doubt one of those species. *See ABF Freight*, 510 U.S. at 323 ("False testimony in a formal proceeding is intolerable.") (citing *United States v. Mandujano*, 425 U.S. 564, 576-77 (1976)). *See also REP MCR Realty v. Lynch*, 363 F.Supp.2d 984, 1013-14 (N.D. Ill. 2005) (noting that lying in a formal proceeding warrants the ultimate sanction of dismissal with

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5. This is a particularly harsh finding, and one the Court is loathe to make; branding someone a liar — particularly in a publicly-available court document — is serious business. Thus, in fairness to Mr. Gorman, the Court notes that its findings today are based on the limited record before it, which may or may not reflect the true nature of Mr. Gorman's character.

prejudice). That the plaintiffs provided an evasive answer to Chrysler's interrogatory about the replacement floor plan financing only bolsters the inescapable conclusion that the case should be dismissed. *See Dotson*, 321 F.3d at 667 ("[I]ncomplete or evasive responses to interrogatories can support, in part, dismissal of the entire action under Rule 37(b).").

3. *The Subordinated Debt & Subordination Agreement*

In its Counterclaim, Chrysler alleged that, on or about December 15, 2000, Midlothian and Mr. Gorman executed a Subordination Agreement in favor of Chrysler. *See* Verified Counterclaim, ¶23. Chrysler further alleged that, under the terms of that agreement, Midlothian agreed to refrain from paying, and Mr. Gorman agreed to refrain from collecting, any payment on a $4.5 million debt owed by Midlothian to Mr. Gorman, which was subordinate in priority to Midlothian's debt to Chrysler. *Id.* In his Answer, Mr. Gorman admitted that these allegations were true. *See* Answer to Verified Counterclaim, ¶23 (attached as Exhibit 105 to Chrysler's Motion for Sanctions for False Statements). In his affidavit submitted in support of the plaintiffs' TRO motion, Mr. Gorman stated that "[a]ttached hereto as Exhibit 8 are true and correct copies of Midlothian's monthly dealer financial statements submitted to defendant. At entry number 262 are circled entries, which clearly show that the amount of the subordinated note had come down by nearly $1 million to just over $3.6 million." Gorman

Affidavit, ¶11. Both of these statements certainly seem to suggest that a $4.5 million debt owed by Midlothian to Mr. Gorman did, in fact, exist.

Despite this, at his deposition, Mr. Gorman testified that there was no $4.5 million loan, that there was no subordinated debt, and that the only reason he had ever signed the Subordination Agreement — subordinating a debt that didn't exist — was to appease the guys at Chrysler who were pushing him to sign it; he claims that the Subordination Agreement was blank when he signed it. *See* Gorman Deposition, pp. 1969-1979, 1988-1994.

Chrysler claims that, if his deposition testimony is to be believed, Mr. Gorman lied in his affidavit when he stated that he had a $4.5 million subordinated note from Midlothian; on the other hand, if his affidavit and Answer to the Counterclaim are to be believed, then Mr. Gorman lied at his deposition when he denied the existence of any $4.5 million debt owed to him by Midlothian. Either way, Chrysler argues, Mr. Gorman has lied, under oath, in a court proceeding, and should be sanctioned.

In his opposition to Chrysler's sanctions motion, Mr. Gorman argues that Chrysler is taking his testimony out of context. He claims that, in his Answer to the Counterclaim, he admitted the *existence* of the Subordination Agreement, but said nothing about whether the agreement was valid and enforceable. But even if his answer could technically be read that way, his affidavit would seem to assume the existence of a

$4.5 million loan, making his affidavit, at best, misleading. If the debt did not exist, Mr. Gorman should have said so in his affidavit — he admitted as much at his deposition, *see* Gorman Deposition, p. 1993; instead, he chose to highlight the fact that the supposed non-existent debt was going down.

Although this statement, like the others, contributes to the erosion of the judicial system caused by litigants who play fast and loose with the truth — no small harm to be sure, the Court is unable to discern any specific harm to Chrysler resulting from the misrepresentations about this subordinated debt. This statement, unlike the statements relating to the capital investment and the alleged attempts to obtain replacement floor plan financing, does not appear to have played any role in the Court's decision to enter the April 11, 2003 Order; nor does it appear to have caused Chrysler to suffer any financial harm — either the debt existed, in which case it is subordinated in priority to any debt owed to Chrysler, or it did not exist, in which case Chrysler would seem to have one less encumbrance to wrestle with. Thus, this statement alone would likely not justify dismissal of the case. Of course, the statement isn't viewed alone; it must be viewed alongside the other misstatements, half-truths and outright lies evident in Mr. Gorman's written and oral testimony. Which leads to Chrysler's next motion.

Appendix C

B. *The Motion for Sanctions for Failure to Produce/Preserve Evidence*

In its second motion for sanctions, Chrysler claims that the plaintiffs failed to produce and preserve material pieces of evidence. Specifically, Chrysler claims that the plaintiffs failed to turn over the dealerships' computer, which contained much of the dealerships' financial records; Chrysler also claims that the plaintiffs failed to preserve or lost the backup data tapes from the computer, lost the 2000 and 2001 monthly accounting journals and schedules for Marquette, and lost or failed to preserve a portion of the notes Mr. Gorman had supposedly created and kept to document racial slurs and racial discrimination by Chrysler. Chrysler contends that the plaintiffs' failure to produce and preserve this evidence demonstrates the plaintiffs' "abuse of the judicial process," Brief in Support of Motion for Sanctions for Failure to Produce and Preserve Evidence, p. 2, and justifies dismissal of the case with prejudice.

The Federal Rules of Civil Procedure authorize the Court to sanction a party for discovery violations, including the failure to preserve evidence that is material to the litigation. *See* Federal Rule of Civil Procedure 37. "A party has a duty to preserve evidence over which it had control and 'reasonably knew or could reasonably foresee was material to a potential legal action.'" *Wiginton v. Ellis*, No. 02 C 6832, 2003 WL 22439865, at *4 (N.D. Ill. Oct. 27, 2003) (quoting *China Ocean Shipping (Group) Co. v. Simone Metals Inc.*,

1999 WL 966443, at *3 (N.D.Ill. Sept. 30, 1999)). The law does not require a party to take "'extraordinary measures' to preserve all potential evidence"; nor does the law require a party to "preserve every single scrap of paper in its business." *Wiginton*, at *4 (citing *China*, 1999 WL 966443, at *3; *Danis v. USN Communications, Inc.*, No. 98 C 7482, 2000 WL 1694325, at *32 (N.D.Ill. Oct. 20, 2000)). "But a party must preserve evidence that it has notice is reasonably likely to be the subject of a discovery request even before a request is actually received." *Wiginton*, at *4 (citing *Cohn v. Taco Bell Corp.*, No. 92 C 5852, 1995 WL 519968, at *5 (N.D.Ill. Aug. 30, 1995); *Wm. T. Thompson, Co. v. Gen. Nutrition Corp.*, 593 F. Supp 1443, 1455 (D.C. Cal. 1984)).

At the outset, the Court notes that the February 5, 2003 and March 3, 2003 letters — in which Mr. Gorman's attorneys lectured at length Chrysler's attorneys concerning the specific obligations imposed by the law concerning the preservation of evidence — make clear that Mr. Gorman was, or certainly should have been, aware that he had a duty to preserve certain evidence.

1. *The Dealerships' Computer*

Chrysler first claims that, despite its requests for all financial records, whether in paper or electronic form, the plaintiffs willfully failed to produce the computer that sat at Midlothian and contained the dealerships' general ledger, financial records and other business records; in fact, Chrysler claims that, between March and June of 2004, the plaintiffs repeatedly told Chrysler that they

no longer had the computer, when in fact, the computer remained on-site at Midlothian until October 2004, when it was repossessed by the company that had leased it to the plaintiffs. The plaintiffs contend that they never told Chrysler they didn't *have the computer*; rather, they say, they told Chrysler that they didn't *have access to the computer* — a representation they claim was true, even during the March to June 2004 time period.

As noted above, Chrysler was clearly seeking physical access to the dealerships' computer, including the hard drive, in the first half of 2004. And there is some evidence in the record to suggest that, the plaintiffs' representations to the contrary notwithstanding, the computer was actually on-site at the dealership during those months.

At his deposition on June 30, 2004, Mr. Gorman testified that the dealerships used computers to record and maintain their financial records. *See* Gorman Deposition, p. 493 (attached as Exhibit G to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). When asked where the computers were, Mr. Gorman testified that he thought Chrysler Financial had them; if not, he testified that he had no idea what became of them, but that he hadn't "seen any computers lying around the store." *Id.*, pp. 493-494. He testified that he "[had] no idea who's got the actual individual computers that sat at the desk. I have no idea where they're at." *Id.*, p. 496. He admitted that the dealerships were using the computers up until October 2003. *Id.*, p. 496, 504.

But Shawn Temple, who served as the dealerships' CFO, testified at his deposition on December 16, 2004, that Reynolds and Reynolds repossessed the dealerships' computer "about two months ago," in October of 2004; he testified that he was there at the time. Transcript of Deposition of Shawn P. Temple. p. 69, 74 (attached as Exhibit T to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). He testified that, included in the repossession was the mainframe and the servers, which would have held all of the records of the dealership, including the accounting records. Temple Deposition, pp. 69-70. He testified that, prior to the repossession, the computer was sitting in the main office at the dealership. *Id.*, p. 69. Mr. Temple testified that, at the time of the repossession, he received from Reynolds and Reynolds (actually, Reyna Financial Corporation) an order documenting the repossession, and that he had immediately turned over that document to Mr. O'Hara. *Id.*, p. 70, 74.

Certainly, the repossession order would shed some additional light on the issue. But that document does not appear to be before the Court. Nevertheless, based upon Mr. Temple's testimony, the Court finds that the computer was actually on-site until October 2004, and, to the extent the plaintiffs' attempted to tell Chrysler otherwise, they should be sanctioned. And plaintiffs' representations to the contrary notwithstanding, they did tell Chrysler that they *did* not have access to the computer; on April 2, 2004, Mr. O'Hara wrote, in an email to Jeffrey Fink, that "[t]o the extent that there are

remaining items contained in Reynolds & Reynolds computers or databases, my client no longer has access to such computers. . . ." *See* Exhibit 5 to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence.

Moreover, even if some of the responses technically may not have misrepresented the physical location of the computer, those responses were still misleading; the plaintiffs could have — and should have — disclosed that the computer was on-site but that they no longer had access to the Reynolds and Reynolds system. Saying as much would at least have given Chrysler the opportunity to mine the hard drive for any relevant evidence. The plaintiffs' semantics gamesmanship prevented Chrysler from having that opportunity. And, because of that (and because of the outright misrepresentations about the location of the computer), they should be sanctioned.

2. *Backup Tapes & Monthly Accounting Records*

Chrysler also claims that the plaintiffs failed to preserve or lost both the backup data tapes from the dealership's computer and the 2000 and 2001 monthly accounting journals and schedules for Marquette. The plaintiffs claim that they have no idea where these items are, and that they cannot provide what they do not have. Mr. Gorman testified that he did not know what had happened to the journals and schedules; he speculated that they may simply have been tossed out when he sold the Marquette dealership — which happened before the

lawsuit was even filed. If this is the case — and Chrysler has offered nothing to suggest that it is not — the plaintiffs (who were not then plaintiffs) may not yet have had any duty at that time to preserve the documents.

At his deposition, Mr. Gorman was asked about Marquette's monthly journals and schedules for 2000 and 2001. He testified as follows:

> [t]he ones we had, we turned over. I know there's some missing, and I don't know if they got tossed out when we sold the store or if they could still be in the building, and I have no access to it. Chrysler owns the building.
>
> But I don't know where anything is at. When the store was sold, I don't know what they threw out and what they kept.
>
> The store — the store was sold prior to the lawsuit being filed, so I have no idea what the people who went down there kept and threw out. I didn't go down there.

Gorman Deposition, pp. 504-505. Oddly enough, when pressed on the issue of the missing journals and schedules, Mr. Gorman immediately contradicted himself by saying that he *had* actually recently gone to the building.

> Q: As I understand it, Mr. Gorman, you produced monthly journals and schedules

from Marquette for 1999 and 2002, is that your understanding?

A: Yes, sir.

Q: But there are no monthly journals and schedules for the year 2000 and 2001; is that correct?

A: Correct.

Q: Those would be — those include the years in which the fraud deals were -- took place at Marquette, correct?

A: Right. That's why Chris just told me it's imperative we try to find them, and I've looked —

* * *

A: Just as recently as maybe two, three weeks ago, Bill, I went over and checked every square foot of those two buildings for any possible thing. I mean, I — I went there myself.

* * *

A: I searched in there, I searched the [Midlothian] Dodge building, I searched everywhere, and I couldn't find anything else.

Gorman Deposition, pp. 505-506.

Appendix C

With regard to the 2000 and 2001 journals and schedules, one thing is clear: during discovery, Mr. Gorman told Chrysler (through his attorney) that he had seen these specific documents, and that they were included in the documents that were produced to Chrysler; then, at his deposition, he back-pedaled from that representation. It is possible that this was simply a misunderstanding. But, given Mr. Gorman's penchant for half-truths, the Court is skeptical that this is the case — especially given that these specific financial documents would seem to be among the most relevant and material to the claims at issue in this case.

3. *The "Missing Notes"*

In their Complaint, the plaintiffs allege that the Chicago Zone Manager, who was identified as Erv Sirovy, a Chrysler employee who was fired in April 2001, used very explicit racial slurs and expressed extreme racially discriminatory views at meetings with Mr. Gorman and Shawn Temple. *See, e.g.*, Complaint, ¶¶28-39. At his deposition, Mr. Gorman testified that, at some point, based upon an instruction from Mr. Vrdolyak, he started to keep notes of his meetings with Mr. Sirovy, in which Mr. Sirovy supposedly used racial slurs, and he testified that these notes formed the basis of the allegations in the Complaint about Mr. Sirovy's racial hostility and racial slurs. *See* Deposition of Gerald Gorman taken July 13, 2004, p. 653, 684, 704-705, 837 (attached as Exhibit G to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence).

Yet, when asked at his deposition to review the notes and to highlight the places in those notes where he had documented the particular racial slurs he claimed Mr. Sirovy used, he was unable to do so; in fact, he was forced to admit that his notes did not reflect any racial slurs — nor did his notes reflect any meetings with Erv Sirovy. *Id.*, p. 678, 684-686. The lack of evidence might stop some witnesses; it did not stop Mr. Gorman:

> Q: Given that your lawyer, Mr. Vrdolyak, instructed you to prepare handwritten notes of your meetings with Mr. Sirovy where he used these outrageous racial slurs, why are you unable to produce any handwritten notes at this deposition?
>
> A: Well, Shawn took some of the notes. . . . I don't know what happened to them. I am not going to lie to you. I did take notes. I did. If I could find them, I would given them to you. I don't know. I know Shawn took some and I took some.
>
> * * *
>
> Q: And you turned those notes over to your lawyers, didn't you?
>
> A: Yes, sir. I turned these notes over to my lawyer. All the notes I could find I turned over to them.

Appendix C

Q: You turned over notes regarding conversations with Erv Sirovy to your lawyers, correct?

A: No. I never turned them over — I turned these over to my lawyers. When I first talked to the lawyers, I had other notes that we went over. I have not been able to locate those notes. Believe me. If I could find them, I would give them to you.

Gorman Deposition, pp. 690-691, 692-693.

A short while later in the deposition, Mr. Gorman was asked to recall what, exactly, Mr. Sirovy had said at the meetings described in the Complaint, and he testified that he could not:

A: I can't recall, Don, if — you are asking me to recall a meeting that took place three years ago and do it in specific order of what was said and when. I don't have the notes in front of me. I don't — I am trying to do this off memory and I am doing the best I can to recall what was said in the meeting.

Q: You don't have the notes because you lost them, right?

A: Yes, sir.

* * *

A: I know I took notes. I don't know where they are at. I've looked at home thinking I might have taken them home. I have looked through the office. I know there is more notes. I discussed these notes were present when I talked with Mr. O'Hara. I don't know where they are at. If I had them, I would give them to you. I have no reason not to give you the notes.

Q: All right. So you did — but you said under oath that the notes were present, you had them when you talked to Mr. O'Hara, correct?

A: Yes, sir.

Q: And you showed them to Mr. O'Hara, didn't you?

A: I believe we went over the notes in my office the first time I met him, yes, sir.

Q: How many pages were they?

A: I don't know. I would say there's probably — I know Shawn is missing notes and I am probably missing — I don't know. I have to be missing maybe eight, ten pages of notes.

Q: How many pages is Shawn missing?

> A: I don't know. You would have to ask him, but he told me he's missing notes. I didn't specifically ask him how many he is missing, Don.

Gorman Deposition, pp. 836-838.

And thus was born the legend of the "missing notes." Based upon this evidence, in its motion for sanctions, Chrysler claims that the plaintiffs failed to preserve or lost a portion of Mr. Gorman's handwritten notes — obviously a very important piece of evidence, given that the contents of the notes formed, at least in part, the basis for the plaintiffs' Complaint.

In response to the sanctions motion, the plaintiffs contend that there are no "missing notes," and that, to the extent Mr. Gorman gave Chrysler the impression that there were "missing notes," he was mistaken. In fact, to support their story, the plaintiffs have offered a supplemental affidavit from Mr. Gorman, which states that, although Mr. Gorman may have referenced "additional notes," and although he stated that he "lost 8 to 10 pages of notes," he was mistaken. *See* Supplemental Affidavit of Gerald Gorman dated March 14, 2005, ¶¶2-3 (attached as Exhibit F to Plaintiffs' Response to Chrysler's Motion for Sanctions for Failure to Produce and Preserve Evidence). In reality, he states, he was "referring to the five-page typewritten summary of the notes from the meetings with Defendant that was prepared by Shawn Temple," which he claims counsel did not show him at the deposition. *Id.*, ¶¶3-4. Finally,

he states, "[w]ith my memory refreshed by the five-page summary that was not shown to me at my deposition, I do not believe that either Mr. Temple or I have lost any notes." *Id.*, ¶5.

Supplemental affidavits executed to "clear up" issues raised in depositions are often self-serving, convenient and, frankly, fishy; this one is no different. The deposition testimony is entirely inconsistent with what Mr. Gorman wrote in his supplemental affidavit — not only is the physical description of the pages way off (8 to 10 pages of missing handwritten notes versus a 5-page typed summary), but, at the deposition, he specifically raised the issue of Mr. Temple's notes and said — not that they must have been what he was thinking about, but that Mr. Temple was also missing some notes.

On October 6, 2004, Mr. Gorman again sat for a deposition, and he was again asked about the missing notes:

> Q: From the time of your last deposition to today's date, have you searched for those missing handwritten notes of racial slurs made by Erv Sirovy?
>
> A: No, sir, I have not. I forgot. I mean, I really did. I was in Michigan. I had a lot going on in my life. I didn't look for them. I will do that, though. I promise.

Appendix C

Q: And you will deliver them to us the minute you find them?

A: Absolutely. If I find them, I will give them to you, yes, sir.

Gorman Dep., p. 1590. Thus, six months before he signed the supplemental affidavit that reflects his apparent epiphany about Shawn Temple's notes, Mr. Gorman had another chance to clear up the mystery and confusion, to stop the hunt for the missing notes, and he failed to do so. In fact, he failed to do so until after Chrysler filed its motion for sanctions, seeking dismissal of the lawsuit because of the loss of those incredibly relevant and material, but phantom, notes.

All things being equal, Mr. Gorman might be entitled to some benefit of the doubt on the "missing notes"; all things being equal, it might seem feasible that Mr. Gorman simply misremembered things at this deposition. But the testimony on this issue is just one more instance in a long string of instances in which Mr. Gorman has been, at best, deliberately obtuse, and, at worst, completely dishonest, in a formal court proceeding. He lacks credibility and consistently demonstrates a willingness to lie or evade the truth, even under oath.

Appendix C

C. *The Plaintiffs' Track Record*

Beyond what was submitted by the parties in connection with the two sanctions motions, the Court notes that the decision to recommend dismissal as the appropriate sanction is also based, in part, on the history of this case. On December 2, 2003, this Court recommended that Mr. Vrdolyak, who originally represented Mr. Gorman, be disqualified from the case. *See* Report & Recommendation dated December 2, 2003. The Court recommended disqualification — a sanction that, like dismissal, is a harsh and drastic measure to be used rarely, *see, e.g., Schiessle v. Stephens*, 717 F.2d 417, 420 (7th Cir. 1983) — because Mr. Vrdolyak demonstrated a complete lack of respect for Court orders and for the integrity of judicial proceedings, and because of inconsistencies in Mr. Vrdolyak's testimony that made it difficult to believe that he was telling the truth. After considering Mr. Vrdolyak's conduct, the Court discerned "the distinct stench of impropriety." *See* Report & Recommendation, p. 16.

And contributing to that stench was the seemingly underhanded and dishonest way in which he conducted his business transactions with Gerald Gorman. In the disqualification order, the Court noted that Mr. Vrdolyak and Mr. Gorman seemed to have an agreement requiring Mr. Gorman to pay Mr. Vrdolyak $10,000 per month on a debt that was not owed; the Court also noted the blurred lines between the roles Mr. Vrdolyak supposedly played in Mr. Gorman's life and the potential for conflict that existed because of those blurred lines. See Report & Recommendation, pp. 18-19.

Although Mr. Gorman should not be condemned solely because of his association with Mr. Vrdolyak, his testimony and his demonstrated willingness to evade, mislead, and lie, suggest that, like his former lawyer, friend and business associate, he cannot be relied upon to play by the rules of this Court. And the evidence of the sketchy financial dealings between the pair that was elicited in connection with the disqualification motion — prophetic enough in the context of the present motion — certainly supports the Court's findings today that the Vrdolyak-Gorman duo was operating in a less-than-above-board manner with respect to the financial workings of Mr. Gorman's dealerships. Accordingly, based upon the entire history of this case, and the evidence presented to date, the Court finds that dismissal of the case is the only appropriate sanction.

CONCLUSION

For the reasons set forth above, the Court finds that Mr. Gorman made false statements in the affidavit that he filed with the Court on April 9, 2003. Those false statements led, at least in part, to the April 11, 2003 Order requiring Chrysler to extend additional floor plan financing to the plaintiffs, which, in turn, caused Chrysler to suffer additional losses. The Court further finds that Mr. Gorman either lied or misled Chrysler during the discovery that occurred after the Stipulated Order was entered on April 11, 2003, that he either lied to Chrysler or misled Chrysler concerning his "missing notes," and that the plaintiffs, at best, misled Chrysler concerning the dealerships' computer. In light of these

findings, the Court recommends that the district judge grant Chrysler's Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for False Statements [#180] and grant Chrysler's Motion for Sanctions Against Plaintiffs and Counterclaim Defendant Gerald Gorman for Failure to Produce and Preserve Evidence [#181].

Moreover, having concluded, under the circumstances, that a lesser sanction is inappropriate, the Court recommends that the district court dismiss the plaintiffs' Complaint with prejudice. The Court recommends that the district court decline to enter a default judgment on Chrysler's Counterclaim, however, as the dismissal of the Complaint is a harsh enough sanction.

Dated: June 14, 2005

RESPECTFULLY SUBMITTED:

s/ Arlander Keys
ARLANDER KEYS
United States Magistrate Judge

Counsel have ten days from the date of service to file objections to this Report and Recommendation with the Honorable Wayne R. Andersen. *See* Fed. R. Civ. P. 72(b); 28 U.S.C. § 636(b)(1). Failure to object constitutes a waiver of the right to appeal. *Egert v. Connecticut General Life Ins. Co.*, 900 F.2d 1032, 1039 (7th Cir. 1990).

APPENDIX D — RELEVANT PORTIONS OF FEDERAL RULE OF CIVIL PROCEDURE 37

Fed. R. Civ. P. 37

Failure to Make Disclosures or to Cooperate in Discovery; Sanctions

* * *

(b) Failure to Comply with a Court Order.

* * *

(2) Sanctions in the District Where the Action Is Pending.

(A) For Not Obeying a Discovery Order. If a party or a party's officer, director, or managing agent—or a witness designated under Rule 30(b)(6) or 31(a)(4)—fails to obey an order to provide or permit discovery, including an order under Rule 26(f), 35, or 37(a), the court where the action is pending may issue further just orders. They may include the following:

(i) directing that the matters embraced in the order or other designated facts be taken as established for purposes of the action, as the prevailing party claims;

(ii) prohibiting the disobedient party from supporting or opposing designated claims or defenses, or from introducing designated matters in evidence;

(iii) striking pleadings in whole or in part;

(iv) staying further proceedings until the order is obeyed;

(v) dismissing the action or proceeding in whole or in part;

(vi) rendering a default judgment against the disobedient party; or

(vii) treating as contempt of court the failure to obey any order except an order to submit to a physical or mental examination.

* * *

(c) Failure to Disclose, to Supplement an Earlier Response, or to Admit.

(1) Failure to Disclose or Supplement. If a party fails to provide information or identify a witness as required by Rule 26(a) or (e), the party is not allowed to use that information or witness to supply evidence on a motion, at a hearing, or at a trial, unless the failure was substantially justified or is harmless. In addition to or instead of this sanction, the court, on motion and after giving an opportunity to be heard:

(A) may order payment of the reasonable expenses, including attorney's fees, caused by the failure;

(B) may inform the jury of the party's failure; and

(C) may impose other appropriate sanctions, including any of the orders listed in Rule 37(b)(2)(A)(i)-(vi).

* * * *

APPENDIX E — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DENYING PETITION FOR REHEARING FILED MARCH 17, 2008

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago, Illinois 60604

March 17, 2008

No. 06-4140

Before

FRANK H. EASTERBROOK, *Chief Judge*

MICHAEL S. KANNE, *Circuit Judge*

ILANA DIAMOND ROVNER, *Circuit Judge*

RIDGE CHRYSLER JEEP, LLC, and SALES, INCORPORATED,

Plaintiffs-Appellants,

v.

DAIMLERCHRYSLER FINANCIAL SERVICES AMERICAS LLC,

Defendant-Appellee.

Appendix E

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 03 C 760
Virginia M. Kendall, *Judge*

Order

Plaintiffs-appellants filed a petition for rehearing and rehearing en banc on March 5, 2008. No judge in regular active service has requested a vote on the petition for rehearing en banc,* and all of the judges on the panel have voted to denying rehearing. The petition for rehearing is therefore DENIED.

* Judge Flaum did not participate in the consideration of this petition.

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SUPREME COURT, U.S.

(2)

No. 07-1576

In the Supreme Court of the United States

RIDGE CHRYSLER JEEP, LLC,
DOING BUSINESS AS MARQUETTE CHRYSLER JEEP,
AND SALES, INCORPORATED, DOING BUSINESS
AS DODGE MIDLOTHIAN,

Petitioners,

v.

DAIMLERCHRYSLER FINANCIAL SERVICES
AMERICAS LLC, FORMERLY KNOWN AS
DAIMLERCHRYSLER SERVICES NORTH
AMERICA LLC,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals For the Seventh Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the Court should grant certiorari to decide whether dismissal of a lawsuit as a sanction for litigation misconduct must be based on clear and convincing evidence of misconduct, rather than a preponderance of the evidence, when (i) the parties always assumed that a clear and convincing standard applied, (ii) the Seventh Circuit commented that preponderance seemed to be the proper standard but expressly declined to overrule its own precedent requiring clear and convincing evidence, and (iii) the Seventh Circuit concluded that the standard of proof was irrelevant to the outcome of the case because "the district court's findings suffice on any standard." Pet. App. 6a.

2. Whether the Court should grant certiorari to decide the fact-bound question of whether dismissal of the lawsuit at issue here was an abuse of discretion.

RULE 29.6 STATEMENT

Respondent DaimlerChrysler Financial Services Americas LLC (referred to herein as "Chrysler Financial") is a wholly-owned subsidiary of FinCo Intermediate HoldCo LLC, which is a wholly-owned subsidiary of Chrysler Holding LLC. An affiliate of Cerberus Capital Management, L.P. owns 80.1% of Chrysler Holding LLC; the other 19.9% is indirectly owned by Daimler AG, which is a publicly-held corporation organized under the laws of the Federal Republic of Germany.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

RULE 29.6 STATEMENT ii

TABLE OF AUTHORITIES iv

STATEMENT 4

A. The Underlying Lawsuit. 4

B. Plaintiffs' Motion For A TRO. 7

C. At Least Two Of The Representations In Gorman's Affidavit Were False. 9

D. Petitioners Violated A Court Order To Produce Midlothian's Computer. 11

E. Gorman's Missing Notes Provided Additional Support For The Conclusion That Dismissal Was Warranted 13

F. The Magistrate's Report. 15

G. The District Court's Decision. 16

H. The Seventh Circuit's Decision. 19

REASONS FOR DENYING THE PETITION 20

A. There Is No Circuit Split. 20

B. The Burden Of Proof Issue Is Irrelevant To The Outcome Of This Case. 23

C. Petitioners' Second Question Presented Raises Purely Factual Questions That Do Not Warrant Review. 24

CONCLUSION 26

TABLE OF AUTHORITIES

Page(s)

CASES

Coburn v. DaimlerChrysler Services North America, LLC, 289 F. Supp. 2d 960 (N.D. Ill. 2003) 9, 10

Maynard v. Nygren, 332 F.3d 462 (7th Cir. 2003) ..... *passim*

Ty, Inc. v. Softbelly's, Inc., 517 F.3d 494 (7th Cir. 2008) 22, 26

Wade v. Soo Line R.R. Corp., 500 F.3d 559 (7th Cir. 2007) 2, 21, 22

RULES

Fed. R. Civ. P. 37 ..... 22, 24

Seventh Circuit Rule 40(e) 20, 21

MISCELLANEOUS

E. GRESSMAN, K. GELLER, S. SHAPIRO, T. BISHOP & E. HARTNETT, SUPREME COURT PRACTICE (9th ed. 2007) 24

RESPONDENT'S BRIEF IN OPPOSITION

Petitioners contend that there is a conflict in the Circuits concerning the quantum of proof necessary to support dismissal of a federal court action as a sanction for litigation misconduct. Petitioners point out that a number of cases, including *Maynard v. Nygren*, 332 F.3d 462, 468 (7th Cir. 2003), have applied a clear and convincing standard of proof. They argue that in this case a panel of the Seventh Circuit "expressly reject[ed]" *Maynard* and adopted a preponderance of the evidence standard instead. Pet. 8. In fact, the panel here did not purport to overrule *Maynard*, nor did it adopt a preponderance standard. Accordingly, there is no conflict in the Circuits and no basis for granting certiorari on that issue.

As described in greater detail below, the district court in this case applied the evidentiary standard petitioners claim it was required to apply, concluding that there was "clear and convincing evidence" of a pattern of misconduct by petitioners that warranted dismissal. As the court explained:

> This clear and convincing evidence reveals that the Plaintiff, Gorman, lied in an affidavit submitted to the court in order to gain a monetary and strategic advantage over Defendant; misled Defendant as to the existence and location of evidence (the computers) which resulted in that evidence not being available for Defendant's use in these proceedings; and either lost key pieces of evidence (notes of his conversations with Defendant's agents) or fabricated their existence in the first instance, in an effort to bolster his

> position before the court and to inflame the passions of the court and the public.

Pet. App. 37a.

On appeal, both parties assumed that a "clear and convincing" standard of proof applied; their arguments focused on whether the district court's findings of misconduct under that standard were clearly erroneous. In his opinion for the court affirming the judgment, Chief Judge Easterbrook discussed the burden of proof issue *sua sponte*. He suggested that *Maynard* might have been wrongly decided, noting that it did not cite certain decisions by this Court "which hold that heightened burdens of proof do not apply in civil cases unless a statute or the Constitution so requires." Pet. App. 6a. Judge Easterbrook observed that "[n]either a statute nor the Constitution requires an elevated burden for dismissal as a sanction, when the burden in the underlying suit is the preponderance of the evidence." *Id.* But he expressly stopped short of adopting preponderance as the standard, stating that "we need not decide today whether the time has come to overrule *Maynard*, as the district court's findings suffice on any standard." *Id.*

That Chief Judge Easterbrook questioned the viability of *Maynard* both in this case and in his earlier opinion in *Wade v. Soo Line R.R. Corp.*, 500 F.3d 559, 561 (7th Cir. 2007), does not provide a basis for declaring the existence of a Circuit split. Nor would this case provide an appropriate vehicle for deciding the issue even if there were a conflict in the Circuits. Here, the magistrate, the district court and three Seventh Circuit judges all agreed that petitioners' misconduct was sufficiently clear to warrant dismissal even if a clear and convincing standard ap-

plied. Thus, a decision in petitioners' favor on their first question presented would have no impact whatsoever on the outcome of this case.

Petitioners' second question presented also provides no basis for granting review. Petitioners complain that, in the Seventh Circuit at least, dismissal is an over-used sanction that should be invoked only as a last resort. But they point to no principle of law that they claim was improperly applied in this case. Instead, their argument appears to be that, on the facts, their misconduct was not sufficiently egregious to warrant the imposition of dismissal as a sanction. However, the courts below disagreed. In fact, the Seventh Circuit went so far as to describe petitioners as having "behaved like a pack of weasels" during the course of the litigation, concluding that they had forfeited their right to litigate their "dubious" claims of discrimination on the merits. Pet. App. 8a. Petitioners offer no explanation why this Court should grant certiorari to review the entirely fact-bound question of whether that conclusion was adequately supported by the record below.

At the end of their Petition, petitioners contend that the district court should at least have granted them an evidentiary hearing on the various claims of misconduct asserted by respondent. Any argument that petitioners were entitled to a hearing, however, is doubly waived. At oral argument on the motion for sanctions in the district court, the court expressly asked whether it was required to hold an evidentiary hearing. Petitioners did not respond by claiming that a hearing was required, nor did they ever ask for an evidentiary hearing. Instead, they made the tactical choice to argue instead that the record did not support the magistrate's findings. On appeal, petitioners did not argue that they should have been afforded a

hearing in the district court. It was not until virtually the last sentence of their Petition for Rehearing in the Seventh Circuit that petitioners first raised the issue—far too late to preserve it for review in this Court.

STATEMENT

A. The Underlying Lawsuit.

Petitioners owned two Dodge/Chrysler dealerships in the Chicago area, Marquette Chrysler Jeep and Dodge of Midlothian. Counterclaim Answer (R.45) ¶¶ 6-9. Gerald Gorman was the owner and president of both petitioners; he and his wife personally guaranteed petitioners' obligations to respondent Chrysler Financial. *Id.* ¶¶ 62-63. Chrysler Financial provided floor-plan financing to Midlothian and also provided financing to some, but not all, of the dealerships' customers who bought their vehicles through installment contracts. Counterclaim (R.13) ¶¶ 12, 53-55; Complt. (R.1) ¶¶ 17-18.

In early 2001, Chrysler Financial discovered that more than fifty installment contracts it had purchased from Marquette were backed by false credit applications. Counterclaim (R.13) ¶ 56. Chrysler Financial suspected that Marquette employees had been complicit in the fraud, which included overstating the invoice/wholesale value of the vehicle, reporting down payments that were inflated or nonexistent, and naming one of three fictitious companies as the customer's employer. Under the governing agreements, however, Chrysler Financial did not have to prove Marquette's involvement in the fraud to hold it liable for defaults. Marquette had warranted the accuracy of all credit applications it submitted to Chrysler Financial and had agreed to pay for any defaults in contracts backed by materially

inaccurate applications. *Id.* ¶ 55. In February 2001, Marquette signed an agreement with Chrysler Financial acknowledging its liability for all of the fraudulent deals it had entered into. *Id.* ¶ 60, Ex. 19.

In December 2002, Chrysler Financial conducted a "Limited Financial Review" of Midlothian's books and discovered that Midlothian had overstated its working capital by $2 million. Counterclaim (R.13) ¶¶ 37, 41. Among other things, the review turned up evidence that Midlothian had understated its accounts payable and overstated its cash and that Gorman and his CFO had used Midlothian as their own personal piggybank, dipping into cash to pay for a variety of personal expenses. Chrysler Financial also discovered that Gorman had caused Midlothian to repay $1 million of a debt it owed to him, in violation of the terms of a subordination agreement. *Id.* ¶ 43. On December 20, 2002, Chrysler Financial sent a notice of default to Midlothian, warning that its financial statements were materially inaccurate and that it needed an immediate infusion of $2.1 million in permanent capital to maintain a sufficient working capital level. *Id.* ¶¶ 46-47, Ex. 16.

In February 2003, petitioners filed their complaint in this action, accusing Chrysler Financial of racial discrimination. R.1. Although petitioners' owners are white, many of their customers were African-American. Petitioners alleged that Chrysler Financial discriminated against African-American customers in purchasing installment contracts, hurting petitioners' vehicle sales. In support of their redlining allegations, petitioners quoted a litany of racial slurs that they claimed Chrysler Financial employees had used in conversations with Gorman and

other white dealership employees. *See* Pet. 3-6.[1] Petitioners claimed that they had threatened to sue Chrysler Financial over its alleged discrimination and that the limited review Chrysler Financial undertook of Midlothian at the end of 2002 had been designed both to silence them and to coerce payment of the amounts still outstanding on the Marquette fraud deals, which petitioners claimed they had no responsibility to pay. Complt. (R.1) ¶ 131.

Petitioners claimed that Chrysler Financial's alleged misconduct had forced Marquette to sell its dealership in January 2003 and had imposed significant losses on Midlothian. *Id.* ¶¶ 153-55. They sought to recover these losses on the theory that Chrysler Financial had breached its contractual obligations, tortiously interfered with their relationships with prospective vehicle purchasers, and violated state and federal dealer protection statutes. *Id.* ¶¶ 157-94.

On the same day that petitioners filed this lawsuit, their attorneys filed another lawsuit on behalf of a purported class of African-American purchasers whose credit applications had been rejected by Chrysler Financial. *Coburn v. DaimlerChrysler Services North America, LLC*, No. 03 C 759 (N.D. Ill.). Like the complaint in this action, the class complaint

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[1] As explained *infra* at 13-14, Gorman claimed that the lengthy quotations set forth in the complaint were based on contemporaneous notes he had taken of the conversations in question. But when Gorman was unable to find notes verifying all of the statements in the complaint, he testified that he had misplaced or lost 8-10 pages of notes. When respondent sought sanctions as a result of petitioners' failure to preserve crucial evidence, Gorman changed his story, claiming that the notes never existed in the first place.

catalogued at great length the racial slurs allegedly used by Chrysler Financial employees and claimed that Chrysler Financial had a policy of discriminating against African-American applicants. The filing of the class action, which has since been resolved in a settlement in which no money damages were paid to class members, was accompanied by widespread publicity. A32.

Chrysler Financial denied petitioners' allegations of discrimination and counterclaimed against petitioners and the Gormans for $227,270 still owing from Marquette on the fraud deals and $10.2 million due under the floor-plan financing Chrysler Financial had provided to Midlothian. R.13. Chrysler Financial also filed a motion for replevin seeking immediate possession of the vehicles on Midlothian's lot that secured its existing debt. R.16.

B. Plaintiffs' Motion For A TRO.

Petitioners responded to Chrysler Financial's replevin motion by moving for a temporary restraining order and a preliminary injunction to compel Chrysler Financial to continue providing Midlothian with floor-plan financing. R.23. At a hearing on the parties' competing motions, the district court indicated that it was not willing to allow Chrysler Financial to terminate its relationship with Midlothian—which claimed to be "on the precipice of going out of business"—until the serious charges raised in petitioners' complaint were resolved. 1DX Ex. C at 6, 16. The court suggested that a "good interim" solution would be to enter a TRO to maintain the status quo while expedited discovery was conducted. *Id.* at 17. However, the court made it clear that it would not require Chrysler Financial to "writ[e] blank checks" to Midlothian and would take appropriate steps to protect

Chrysler Financial from incurring additional losses. *Id.* at 16. The court suggested that the parties negotiate the terms of an agreed TRO within these guidelines. *Id.* at 12-13, 20-21.

Chrysler Financial argued that it should not be forced to provide financing to Midlothian because the dealership should have been able to find alternative financing from a bank if it were as financially sound as Gorman claimed it to be. Petitioners responded that Gorman had "tried twice" to obtain financing from another source but "because of the litigation has been unsuccessful." *Id.* at 28.

There were also discussions at the hearing about Gorman's assertion that he had already put $1.4 million back into Midlothian since December 2002 when Chrysler Financial had demanded an increase in working capital. Counsel for Chrysler Financial asked petitioners to identify the source of the additional capital and emphasized the need to make sure that it was "unencumbered." *Id.* at 24. Petitioners' counsel responded by stating that "we will sign an affidavit that the money is unencumbered . . . . that there is no loan back, or whatever it is." *Id.*

After the hearing, plaintiffs filed an affidavit signed by Gorman that was designed to assure the court that the TRO was necessary and that Chrysler Financial's interests would be protected. R.29. In the affidavit, Gorman testified that "I went to two different banks to try to take out a loan and to refinance the floor plan at Midlothian. I was turned down by both banks due to issues related to the financial hold and pending litigation with defendant." *Id.* ¶ 12. He also testified that in December 2002 approximately $925,000 in "additional working capital" had been invested in the Midlothian dealership, that it was a

"capital investment," which was "unencumbered," and that the "source of the capital investment was not a loan from a third party that would require repayment from dealership assets, nor was it a withdrawal from a bank account." The affidavit identified the sources of this "capital investment" as "monies obtained from the sale of stock certificates and a direct investment from a long time business associate." *Id.* ¶ 2.

After the affidavit was filed, the court entered a stipulated TRO that required Chrysler Financial to continue supplying Midlothian with floor-plan financing for a period of 180 days. 1DX Ex. O. Paragraph 9 of that Order provided that "Midlothian represents and warrants that a $925,000 equity capital infusion has been made, which is unencumbered and not . . . subject to repayment by Midlothian to the investment source." *Id.*

C. At Least Two Of The Representations In Gorman's Affidavit Were False.

The district court concluded that there was clear and convincing evidence of two "distinct misrepresentations" in Gorman's affidavit. Pet. App. 30a.

First, the "capital investment" Gorman testified Midlothian had received from a "long time business associate" was not a "capital investment" at all, but rather a loan from Edward R. Vrdolyak, who at the time was one of plaintiffs' attorneys. 1DX, Ex. D.[2] Af-

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[2] Vrdolyak was later disqualified in both the *Coburn* case and this case. *See Coburn v. DaimlerChrysler Services North America, LLC*, 289 F. Supp. 2d 960 (N.D. Ill. 2003). R.102 at 19. In his opinion disqualifying Vrdolyak in this case, the magistrate judge stated that he was troubled, not only by unethical contacts Vrdolyak had with a Chrysler Financial employee, but also by his "questionable" business dealings with Gorman pur-

ter months of effort and a successful motion to compel, Chrysler Financial finally obtained a copy of the check Vrdolyak had written for $750,000 made payable to "Midlothian Dodge," which was described in the memo section as a "LOAN." *Id.* Vrdolyak also produced a hand-written agreement documenting a $750,000 "loan from Edward R. Vrdolyak to the aforesaid Midlothian Dodge." 2DX Ex. 65. The agreement provided that the loan would be collateralized by Midlothian's used car inventory. *Id.* In addition, as the magistrate found, "to the extent payments were being made on that loan, they were being made out of the coffers of the dealership, not out of Mr. Gorman's personal coffers." Pet. App. 66a.

On appeal, petitioners conceded that the affidavit "may have been inaccurate" in certain respects, but argued that the inaccuracies were immaterial because, after the loan agreement was signed, Vrdolyak had orally agreed to give up his lien on Midlothian's inventory and he and Gorman had supposedly agreed to treat Gorman, rather than Midlothian, as the obligor on the loan. Petitioners' Seventh Circuit Br. at 18. As the Seventh Circuit noted in its opinion, petitioners' explanation "is unhelpful, even if true, for Gorman assured Judge Andersen that he had raised new equity capital" from a third party, rather than taking out a loan. Pet. App. 6a. In any event, the Seventh Circuit concluded that the district court's finding that Midlothian remained the obligor on the loan was not clearly erroneous in light of the clear documentary evidence of a loan to the dealership and the admitted fact that the only loan payments had come from Midlothian. Pet. App. 6a-7a.

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suant to which Vrdolyak received $10,000 a month from the dealership "in exchange for, essentially, nothing." *Id.*

Second, the district court concluded that there was also clear and convincing evidence that Gorman had lied when he testified in his affidavit that he had twice tried and failed to obtain floor-plan financing from another source after Chrysler Financial put Midlothian on financial hold in December 2002. *Id.* at 26a, 31a. The magistrate branded this statement as the "most blatant of the lies alleged," *id.* at 74a, because during the course of discovery petitioners admitted that Gorman had not contacted any potential lenders until *after* the TRO was entered. 1DX Ex. G at 2584-86. After the motion for sanctions was filed and Gorman realized that he had effectively confessed to perjuring himself in his affidavit, he attempted to remedy the situation by submitting another affidavit claiming that he had spoken with one bank before the hearing. But, as the Seventh Circuit noted, the "district court didn't have to buy the latest story." Pet. App. 7a.

D. Petitioners Violated A Court Order To Produce Midlothian's Computer.

The district court also concluded that there was clear and convincing evidence that petitioners had misled respondent about the whereabouts of Midlothian's computer, in violation of a court order requiring them to produce the computer and all of their computerized records. Early on in the litigation, Chrysler Financial served document requests asking petitioners to produce all of their general ledger and accounting information, both in paper and electronic form. 2DX Exs. 1 (at 9-10) and 2 (at 12-13). Although petitioners eventually produced documents in response to this request, there were many obvious gaps in their production, which included the most crucial time periods that were at issue in the lawsuit.

Respondent's counsel spent months trying to track down the missing information. When respondent asked for financial information on discs or hard drives, petitioners' counsel responded that petitioners had none. 2DX Ex. 5. They also told respondent that Midlothian, which had gone out of business, no longer had "access" to computerized information systems that it had leased from a company called Reynolds & Reynolds. 2DX Ex. 4.

On April 30, 2004, the magistrate entered an order requiring plaintiffs to produce "the monthly accounting journals and schedules for the years 2000 and 2001, and the electronic records of Midlothian called the Reynolds & Reynolds materials, including the tapes, printouts and any other financial material stored in their computers." R.127. When this order was issued, the Midlothian computer was still on the dealership's premises. It remained there for another five months until October 2004, when it was finally repossessed. 1DX Ex. T-2 at 68. Nevertheless, plaintiffs never revealed the computer's whereabouts. Instead, they continued to claim that they had no "access" to the computer. *See* 2DX Ex. 7.[3] It was not until the end of discovery, when the computer was already long gone, that Midlothian's former CFO

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[3] The district court concluded that Gorman lied when he was asked about the computer's whereabouts in his June 2004 deposition. Pet. App. 32a. Although petitioners concede that the computer was still in its usual spot at the dealership at that point in time, Gorman testified that he had no idea what had become of the computer or its hard drive. He also testified that he had just recently been at the Midlothian offices and had "checked every square foot of those two buildings for any possible thing," but had not seen "any computers laying around the store," and that his CFO had searched for the computers and been unable to find them. 1DX Ex. G at 494-505.

finally disclosed in deposition testimony that the computer had been on the premises until October 2004. *See* 1DX Ex. T at 74.

The magistrate concluded that petitioners had at the very least "misle[d]" Chrysler Financial about the whereabouts of Midlothian's computer by engaging in "semantic[] gamesmanship." Pet. App. 83a. The district court agreed, concluding that there was clear and convincing evidence that plaintiffs "concealed the true nature of the location of [their] computers by stating in April 2004 that they did not have access to the computers," when they were admittedly still on-site at the Midlothian dealership. *Id.* at 32a. "[E]ven giving Plaintiffs the benefit of their interpretation" of what "access" meant, the court found that "their incomplete answer regarding lack of access was given to mislead Defendant into believing that the computers were not in existence." *Id.*

E. Gorman's Missing Notes Provided Additional Support For The Conclusion That Dismissal Was Warranted.

The centerpiece of petitioners' complaint was a series of lengthy block quotes of statements allegedly made by Chrysler Financial employees in which they purportedly used a variety of racial slurs and openly admitted to discriminating against petitioners' African-American customers. *See, e.g.*, Complt. (R.1) ¶¶ 28-29. At his July 2004 deposition, Gorman testified that when these types of statements had first surfaced, his attorney had advised him to take contemporaneous notes of the meetings. 1DX Ex. G at 653-54. In response to Chrysler Financial's discovery requests, petitioners had produced some of Gorman's handwritten notes. At the deposition, defense coun-

sel asked Gorman to identify where particular statements alleged in the complaint were documented in those notes.

When Gorman was unable to find any reference in his notes to certain alleged statements, he testified that he had taken notes but that they must have been lost or even stolen: "I know I took notes from a couple of meetings. I don't know if I misplaced them. I've looked, but my office [was] never locked." *Id.* at 690. *See also id.* at 694 ("we did have some notes that I have not been able to find"); *id.* at 705 ("I had notes that I can't find"). When pressed about the missing notes, Gorman testified that "I have to be missing maybe eight, ten pages of notes." *Id.* at 838. Gorman testified that he had already searched for and been unable to find his missing notes: "I've looked at home thinking I might have taken them home. I have looked through the office. I know there is more [*sic*] notes." *Id.* at 837.

Gorman was deposed in both this case and the discrimination case brought on behalf of petitioners' customers. At each deposition, Gorman told a consistent story—that he had made 8-10 pages of handwritten notes that would have supported the allegations of the complaint, but that he had not been able to locate those notes despite a diligent search. When Chrysler Financial moved for sanctions based on petitioners' failure to preserve critical evidence, however, Gorman's story suddenly changed. He submitted a "supplemental affidavit" claiming that he had been confused at (apparently all of) his deposition sessions by the way he was questioned, that he had not personally made 8-10 pages of additional handwritten notes, that he had not lost any notes, and that, when he referred to 8-10 pages of his own handwritten notes, he had actually been thinking

about a typed, 5-page summary that his former CFO had written, which had been produced to Chrysler Financial. 1PX A-36.

The magistrate found Gorman's affidavit "self-serving, convenient and, frankly, fishy." Pet. App. 91a. Given Gorman's track record of being "at best, deliberately obtuse, and, at worst, completely dishonest, in a formal court proceeding," the magistrate concluded that the missing notes were yet another factor supporting dismissal as a sanction. *Id.* at 92a.[4]

The district court agreed with this analysis and concluded that clear and convincing evidence showed that Gorman "either lost key pieces of evidence (notes of his conversations with Defendant's agents) or fabricated their existence in the first instance, in an effort to bolster his position before the court and to inflame the passions of the court and the public." *Id.* at 37a.

F. The Magistrate's Report.

After discovery closed, Chrysler Financial filed a motion for summary judgment on all of plaintiffs' claims. R.183. At the same time, it filed two motions

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[4] Gorman's "track record" of dishonesty includes his admission that two dealership applications he had submitted to Daimler-Chrysler contained a variety of misstatements. In those applications, Gorman falsely claimed to have graduated from the University of Arizona with a degree in biochemistry and to have completed two years of medical school; he also gave inaccurate answers to questions about his employment history to conceal the fact that he had been barred from working in the securities industry. R. 265, Ex. 15 at 239-67. Gorman characterized these misrepresentations as "oversights" and disclaimed responsibility for them, although he acknowledged that he had signed the documents. *Id.* at 242, 255.

for sanctions, seeking dismissal of petitioners' complaint with prejudice and the entry of judgment on its counterclaim on two separate grounds: (1) that petitioners had made false statements during the proceedings on their motion for a TRO (R.180) and (2) that petitioners had intentionally failed to preserve and produce critical evidence (R.181).

The sanctions motion was referred to Magistrate Judge Keys, who issued a 48-page report and recommendation. As described above, Judge Keys concluded that Gorman's affidavit contained two false statements which led "at least in part, to the April 11, 2003 Order requiring Chrysler to extend additional floor plan financing to the plaintiffs which, in turn caused Chrysler to suffer additional losses." A80-81. He concluded that "[d]eliberately providing false information to the Court to achieve one's objective cannot be condoned and certainly warrants the harshest of sanctions." Pet. App. 75a.

In addition, Judge Keys found that Gorman "either lied or misled Chrysler during the discovery that occurred after the Stipulated Order was entered." *Id.* at 94a. The magistrate recommended dismissal of the complaint as the appropriate sanction for petitioners' misconduct, noting that in light of Gorman's "demonstrated willingness to evade, mislead, and lie. . . he cannot be relied upon to play by the rules of this Court." *Id.*

G. The District Court's Decision.

Petitioners filed timely objections to Judge Keys' report. R.261. After those objections were briefed, the case was transferred from Judge Andersen, who had presided over the TRO hearings, to Judge Kendall. R.274.

The district court held oral argument on petitioners' objections in February 2006. R.280. At that hearing, the court asked whether it was required to have a "testimonial hearing in order to make my own determination as to whether or not" Gorman and petitioners had been telling the truth. Supp. R., 2/24/06 Tr. at 16. Petitioners did not argue that a hearing was required, nor did they ever file a motion asking the court to convene an evidentiary hearing on the sanctions motions.

Ultimately, the district court issued a 26-page opinion reviewing the record de novo and concluding that there was clear and convincing evidence of two false statements in Gorman's affidavit and of willful concealment of evidence as a result of plaintiffs' failure to turn over the Reynolds & Reynolds computer during discovery. Pet. App. 26a. The court also concluded that the other issues raised by Chrysler Financial in its sanctions motion—including the missing notes—provided additional support for the conclusion that "the case had been tainted with discovery violations and at least misleading statements throughout its course." *Id.*

On the issue of remedy, the district court stated that dismissal can be imposed as a sanction only where there is "clear and convincing evidence" of "contumacious conduct" or discovery violations where the "offending party has demonstrated wilfulness, bad faith, or fault." *Id.* at 27a, 36a. The court noted the factors that must be weighed in choosing between dismissal and a lesser sanction: prejudice to the defendant, prejudice to the judicial system and the need for deterrence and punishment. *Id.* The court concluded that all of these factors weighed in favor of dismissing petitioners' complaint. First, it

concluded that "[t[here is no doubt that Chrysler has been prejudiced by the conduct of Plaintiffs throughout this case." *Id.* at 39a. That prejudice included not only being forced to provide floor-plan financing to Midlothian for an additional six months, which imposed an additional loss of $500,000 on Chrysler Financial, but also losing access to discovery materials that were the "key elements to Chrysler's defense." *Id.*

Second, the district court concluded that the prejudice to the legal system "merits the harsh sanction of dismissal." *Id.* Prior sanctions imposed on petitioners during the course of discovery had not had any deterrent effect.[5] Moreover, petitioners' evasive conduct during discovery, including their efforts to avoid revealing Vrdolyak's role in financing Midlothian, were "not the actions of truth-seeking individuals intent on having their day in court, but rather, sleight of hand tactics of manipulators seeking to use the federal court system to their own advantage." *Id.* at 39a-40a. Even without prejudice to respondent, the court concluded that petitioners' "flagrant violations" would be enough to support dismissal of the case. *Id.*

Finally, the district court concluded that the lesser sanctions petitioners had proposed—such as fines or adverse jury instructions—would be inade-

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[5] The court had granted a number of motions to compel and had awarded attorneys' fees to respondent. R.101. Judge Keys had also ordered Gorman to submit to an additional deposition on damages and ordered petitioners to pay all of the costs of that additional deposition, including respondent's attorneys' fees. R.139. When petitioners identified a damages expert months after the deadline for doing so had passed, Judge Keys struck their expert. R.169.

quate. The court concluded that the harm to petitioners from dismissal "is more than outweighed by the harm to Chrysler and to the legal system as a whole that would flow from any decision to allow Plaintiffs to continue to prosecute their case." *Id.* at 41a.

H. The Seventh Circuit's Decision.

Petitioners appealed to the Seventh Circuit, arguing that the district court's findings were clearly erroneous and that, even if those findings were justified, they did not warrant dismissal of the complaint as a sanction for misconduct. In briefing the appeal, both sides assumed that only clear and convincing evidence of misconduct would suffice to support a dismissal sanction.

The Seventh Circuit affirmed. The panel concluded that the district court's findings were not clearly erroneous, whether a preponderance or a clear and convincing standard was applied. Pet. App. 6a. Petitioners' arguments on the facts were rejected as "uniformly unconvincing." *Id.* And the court found no abuse of discretion in the district court's selection of dismissal as a sanction. It acknowledged that the "penalty must be proportional to the wrong," but concluded that this principle did not help petitioners: "One who misuses litigation to obtain money to which he is not entitled is hardly in a position to insist that the court now proceed to address his legitimate claims, if any there are." *Id.* at 8a.

The court rejected petitioners' argument that they were entitled to have their claims of discrimination decided on the merits. In light of Gorman's inability to produce the notes he claimed to have made, the court found those claims to be "dubious." *Id.* Having "behaved like a pack of weasels," petitioners

"can't expect any part of their tale be believed." *Id.* In any event, the court noted that any discrimination was actionable by the victims of the alleged discrimination—petitioners' customers, on whose behalf a complaint had already been filed and settled. "The dealerships are only incidental losers (if discrimination occurred at all), and this suit need not be kept alive on that account." *Id.* at 8a-9a.

REASONS FOR DENYING THE PETITION

A. There Is No Circuit Split.

The Petition rests on the erroneous assumption that the Seventh Circuit adopted a preponderance of the evidence standard of proof in this case, thus creating a split with decisions in other Circuits that have required clear and convincing evidence of misconduct to uphold dismissal as a sanction. In support of their claim of a circuit conflict, petitioners quote the portion of the opinion that criticizes the Seventh Circuit's adoption of a clear and convincing standard five years ago in *Maynard v. Nygren*. But petitioners inexplicably ignore the fact that the panel here expressly declined to decide "whether the time has come to overrule *Maynard*" because it was unnecessary to do so since "the district court's findings suffice on any standard." Pet. App. 6a. Because *Maynard* remains the law in the Seventh Circuit, there is simply no conflict for this Court to resolve.

That *Maynard* is still good law is apparent not only from the decision in this case, but also from the Seventh Circuit's own rules. The panel in this case could not have simply overruled the earlier panel decision in *Maynard*. Instead, if a proposed opinion approved by a panel adopts "a position which would overrule a prior decision of this court," Circuit Rule 40(e) requires the opinion to be circulated among the

active members of the court, who then have an opportunity to vote to rehear the issue en banc. When this procedure is followed and a majority of the active judges acquiesce in overruling the court's prior precedent, the opinion is required to carry a footnote to that effect. *Id.* Here, there is no such footnote and nothing else in the opinion to suggest that (contrary to its explicit statement) the panel here intended to overrule *Maynard sub silentio.*

Indeed, it is unclear whether the Seventh Circuit will *ever* choose to overrule *Maynard.* Chief Judge Easterbrook is plainly interested in the burden of proof issue. He raised it *sua sponte* in *Wade v. Soo Line R.R. Corp.*, 500 F.3d at 561, which was issued after briefing in this case had been completed, but before oral argument. In *Wade*, Judge Easterbrook "doubt[ed] that 'clear and convincing' evidence is required" to uphold dismissal as a sanction, but noted that the appellee had not "asked us to revisit *Maynard* . . . and use the preponderance standard, perhaps because the evidence of bad faith is manifest." *Id.* Similarly, in this case, respondent did not ask the court to revisit *Maynard*, instead arguing that there was ample evidence to support the district court's conclusion that there was clear and convincing evidence of the kind of misconduct necessary to warrant dismissing the complaint. Thus, although Chief Judge Easterbrook has twice voiced his doubts about whether *Maynard* employed the correct burden of proof, he still has not had the benefit of hearing argument on both sides of the issue. As a result, it is impossible to say that even he would ultimately vote to overrule *Maynard* by adopting a preponderance standard—particularly if doing so would, as petitioners contend, create a split in the Circuits.

Contrary to petitioners' argument, Judge Posner's opinion for the court in *Ty, Inc. v. Softbelly's, Inc.*, 517 F.3d 494 (7th Cir. 2008), does not indicate any confusion over the burden of proof issue in the Seventh Circuit. *Ty, Inc.*, which was issued two days after the decision in this case, canvasses the law on burden of proof in cases where sanctions are sought. It notes that clear and convincing evidence is ordinarily required to prove fraud, including fraud on the court. *Id.* at 498. It then cites cases, including *Maynard*, suggesting that clear and convincing evidence is required to impose "*any* substantial sanction for misconduct in litigation," whether or not fraud was involved. *Id.* (emphasis in original). Judge Posner observed that *Maynard* involved Rule 37 and that its "soundness was questioned in *Wade*." *Id.* He then went on to discuss the burden of proof in a case like *Ty, Inc.*, where the court's power to sanction was based on its inherent authority.

After considering the function served by the "tripartite division of burdens of proof," Judge Posner voiced his "doubt" as to "whether there is any utility in insisting on proof by clear and convincing evidence in a case such as this . . . and if not whether there should nevertheless be a category of litigation sanctions that require a heightened standard of proof." *Id.* at 499. But, as in this case and in *Wade*, Judge Posner found it unnecessary "to resolve our doubts" because the outcome of the appeal would be the same regardless of whether a preponderance or clear and convincing burden of proof was imposed. *Id.*

Ty, Inc. confirms that it is impossible to tell how the Seventh Circuit would come out if the burden of proof issue were actually argued by the parties in a case where the choice between clear and convincing evidence and preponderance mattered to the outcome

of the appeal. It is possible that *Maynard* might be overruled. It is also possible that the Seventh Circuit might adopt differing burdens of proof for different types of sanctions and that, on close examination, there might be no conflict at all with decisions in other circuits. Yet another possibility is that a majority of the judges in active service would decide that *Maynard* should not be overruled.

Unless and until the Seventh Circuit takes some action to overrule *Maynard*, however, there is no basis for any claim of conflict, either among the Circuits or within the Seventh Circuit, and no need for this Court to take any action to clarify the burden of proof issue. District courts in the Seventh Circuit are required to continue following *Maynard*. As a result, the rule that petitioners claim is the right rule—that dismissal is permissible only if misconduct has been proven by clear and convincing evidence—continues to apply throughout the Circuit.

B. The Burden Of Proof Issue Is Irrelevant To The Outcome Of This Case.

Even if Chief Judge Easterbrook's ruminations about burden of proof could somehow be contorted into a circuit split, this case would not provide an appropriate vehicle to resolve the purported conflict. The outcome here would not change even if this Court were to conclude that clear and convincing evidence of misconduct is required to uphold dismissal as a sanction. The district court decided that misconduct had been established by clear and convincing evidence. And the Seventh Circuit concluded that the district court's findings were not clearly erroneous, even assuming that a heightened burden of proof applied.

That the outcome does not depend on the resolution of the principal question petitioners have presented would be reason enough to deny the Petition even if there were a clear conflict between the Circuits. *See* E. GRESSMAN, K. GELLER, S. SHAPIRO, T. BISHOP & E. HARTNETT, SUPREME COURT PRACTICE at 248 (9th ed. 2007).

C. Petitioners' Second Question Presented Raises Purely Factual Questions That Do Not Warrant Review.

It is not clear what legal question petitioners seek to raise in their second question presented. Petitioners acknowledge that Rule 37 "grants a court the power to dismiss a case as a sanction for noncompliance with a discovery order." Pet. 21. They also agree that "[i]t is well settled that a court may dismiss an action as a sanction" by invoking its inherent powers. *Id.* Petitioners argue that this power must be exercised with "restraint and discretion." But they offer no basis for concluding that the courts below failed to adhere to these principles.

Petitioners complain that the Seventh Circuit has allowed trial courts to "[r]outinely resort[]" to dismissal as a sanction. Pet. 22. But petitioners cite no statistics to support that conclusion. Nor do they articulate any new or different legal principle they claim this Court should adopt to alter the way in which the Seventh Circuit or other Courts of Appeals approach appeals from orders dismissing a lawsuit as a sanction for litigation misconduct.

Instead, petitioners' argument boils down to the assertion that dismissal was inappropriate under the particular facts of this case. For example, petitioners contend (at 17) that the court here failed to properly

apply the concept of proportionality. The decision, however, plainly recognizes the *principle* of proportionality. *See* Pet. App. 8a ("the penalty must be proportionate to the wrong"). Petitioners' only quarrel is with how that principle was applied to the particular facts of this case. Petitioners argue that the Seventh Circuit arrived at the right result in *Ty, Inc.*, where it overturned a dismissal sanction, while reaching the wrong result here. But the different outcomes can be fully explained by the difference in the facts. In *Ty, Inc.*, the defendant admitted that it had suffered no prejudice apart from attorneys' fees as a result of a single instance of misconduct by the plaintiff. 517 F.3d at 498, 500. Here, by contrast, the district court found that petitioners' repeated misconduct had not only caused respondent to lose an additional $500,000-plus on the Midlothian dealership, but had also effectively hamstrung respondent's defense.

Petitioners further contend that it was error to allow respondent to use Gorman's deposition testimony as the basis for its sanctions motions. Pet. 22. Petitioners contend that respondent should have been relegated instead to using Gorman's various admissions, lies and evasions in his deposition testimony as impeachment at trial. But petitioners cite no legal principle that would preclude a court from considering deposition testimony given under oath in ruling on a motion for sanctions. Instead, petitioners appear simply to be repeating their factual assertion, made and rejected below, that it was "entirely understandable" that Gorman would become "confused" and contradict himself during a lengthy deposition. *See* Petitioners' Seventh Circuit Reply Br. at 5.

Finally, petitioners contend that the district court should have at least held an evidentiary hearing before granting respondent's sanctions motions. Once again, however, petitioners do not contend that an evidentiary hearing is *always* required before a complaint can be dismissed as a sanction; instead, they contend that a hearing should have been held under the facts of this particular case. But any such argument has been doubly waived. Petitioners did not ask the district court to hold an evidentiary hearing, even when the district court raised the issue. And they waived the issue a second time by failing to challenge the lack of a hearing in the Seventh Circuit until they filed their petition for rehearing.

In any event, petitioners had their day in court and then some. They filed voluminous briefs before the magistrate and the district court, both of whom carefully considered all of the various explanations petitioners offered for their conduct during the course of the litigation. The magistrate and the district court both concluded that there was clear and convincing evidence that petitioners had lied to the court and misled respondent in discovery, prejudicing not only respondent's interests but the interests of the legal system as well. On appeal, the Seventh Circuit reviewed these findings regarding "Gorman's chicanery" and found that they were adequately supported. Pet. App. 8a. Petitioners offer no reason why this Court should delve into the complex facts outlined above in order to second-guess that entirely fact-bound conclusion.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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